11 Am. Jur. 2d Bills and Notes VII A Refs.

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

A. In General

Topic Summary | Correlation Table

Research References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 313, 315, 441.1 to 443, 474, 488, 496(3)

A.L.R. Library

A.L.R. Index, Bills and Notes
A.L.R. Index, Uniform Commercial Code (UCC)
West's A.L.R. Digest, Bills and Notes 313, 315, 441.1 to 443, 474, 488, 496(3)

End of Document

11 Am. Jur. 2d Bills and Notes § 205

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

A. In General

§ 205. Persons entitled to enforce negotiable instruments, generally

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 441.1 to 443

The term "persons entitled to enforce" an instrument means:
(1) the holder of the instrument;[1]

(2) a nonholder in possession of the instrument who has the rights of a holder;[2] or
(3) a person not in possession of the instrument who is entitled to enforce the instrument pursuant to those sections of the Uniform Commercial Code governing lost or destroyed instruments and payment or acceptance by mistake.[3]
A person may be a person entitled to enforce the instrument even though that person is not the owner of the instrument or is in wrongful possession of it.[4]

The plaintiff's status as a holder of the instrument, or as a nonholder with the rights of a holder, is an element of an action to enforce a negotiable instrument.[5] If a check is transferred with a missing indorsement, the transferee is a person entitled to enforce the instrument, as a nonholder in possession of the check, if the transferor had the right to enforce it.[6] Thus, if the Federal Deposit Insurance Corporation (FDIC) finds an instrument in the possession of a bank of which the FDIC became the receiver, and the bank was clearly a holder, the FDIC and its transferees acquire the rights of a holder and may enforce it,[7] and the FDIC must, at a minimum, prove a sufficient transfer from a holder to the FDIC, and produce the instrument at trial.[8]

Footnotes

1 U.C.C. § 3-301(i)[Rev].
As to the definition of a holder, see § 206.

2 U.C.C. § 3-301(ii)[Rev].
To be a "non-holder in possession" of a mortgage note who has the rights of a holder, the alleged possessor must have a note that has not been indorsed either by special indorsement or blank indorsement; basically, no negotiation has

occurred because the person now in possession did not become a holder by lack of the note being indorsed. Deutsche Bank Nat. Trust Co. v. Richardson, 2012 OK 15, 273 P.3d 50 (Okla. 2012).
As to a subsequent transferee acquiring the transferor's rights, see § 210.

[3] U.C.C. § 3-301(iii)[Rev].
As to the enforcement of lost or destroyed instruments, see §§ 271 to 278.
As to payment or acceptance by mistake, see § 481.

[4] U.C.C. § 3-301[Rev].
As to the distinction between a holder and an owner, see § 206.

[5] Ninth RMA Partners, L.P. v. Krass, 57 Conn. App. 1, 746 A.2d 826, 41 U.C.C. Rep. Serv. 2d 585 (2000) (observing that the failure to so allege is a ground for a motion to strike the complaint, and the failure to prove this results in judgment for the defendant, but holding that the defendants waived the point, which was not jurisdictional).

[6] In re McMullen Oil Co., 251 B.R. 558, 42 U.C.C. Rep. Serv. 2d 507 (Bankr. C.D. Cal. 2000).

[7] Ninth RMA Partners, L.P. v. Krass, 57 Conn. App. 1, 746 A.2d 826, 41 U.C.C. Rep. Serv. 2d 585 (2000).

[8] F.D.I.C. v. Houde, 90 F.3d 600, 30 U.C.C. Rep. Serv. 2d 549 (1st Cir. 1996) (decided under prior Article 3 and holding that result is the same under both versions of Article 3).

End of Document

11 Am. Jur. 2d Bills and Notes § 206

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

A. In General

§ 206. Holder of negotiable instrument defined; owner distinguished

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 443

Forms

Forms relating to holder of instrument, generally, see Am. Jur. Pleading and Practice Forms, Commercial Code [Westlaw®(r) Search Query]

A "holder" is the person in possession of a negotiable instrument that is payable either to bearer, or to an identified person that is the person in possession.[1] A payee of an instrument in his or her possession is always a "holder."[2]

Comment:

Where an instrument is payable to X and Y, neither X nor Y acting alone is the person to whom the instrument is payable,[3] so neither person, acting alone, can be the holder of the instrument. The instrument is one "payable to an identified person," X and Y jointly, and neither individually is the identified person in the instrument, so neither can enforce it.[4]

By definition, possession of the paper by the claimant is essential to the claimant having the status of holder.[5] A person who is not in possession of an instrument is not a holder and, except as provided by the Code,[6] does not have the right to enforce

the instrument.[7]

Observation:

The status of holder of an instrument is significant only if the creditor is attempting to enforce the instrument itself, as opposed to the underlying obligation.[8]

The question of ownership of the instrument is irrelevant to the determination whether the plaintiff is the holder with the right to enforce the instrument.[9]

Footnotes

1 U.C.C. § 1-201(b)(21)(A)[Rev].
When a party can show it is an "identified person" by the "negotiation" of a note to it, and to each of its successors, it may enforce the note as a "holder." In re Stanley, 514 B.R. 27 (Bankr. D. Nev. 2012) (under Nevada law).

2 New Bedford Inst. for Sav. v. Gildroy, 36 Mass. App. Ct. 647, 634 N.E.2d 920, 25 U.C.C. Rep. Serv. 2d 450 (1994); Edwards v. Mesch, 1988-NMSC-085, 107 N.M. 704, 763 P.2d 1169, 7 U.C.C. Rep. Serv. 2d 801 (1988).
A finance company that had purchased a promissory note from the Federal Deposit Insurance Corporation was the holder, with the right to enforce the instrument, even if the FDIC had reacquired ownership of the note and its delivery of the note to the finance company was inadvertent, since company was in possession of a note that was payable to itself. SMS Financial, Ltd. Liability Co. v. ABCO Homes, Inc., 167 F.3d 235, 42 Fed. R. Serv. 3d 1214, 37 U.C.C. Rep. Serv. 2d 1200 (5th Cir. 1999).

3 § 61.

4 U.C.C. § 3-110[Rev] Official Comment 4.

5 Hanalei, BRC Inc. v. Porter, 7 Haw. App. 304, 760 P.2d 676, 7 U.C.C. Rep. Serv. 2d 1528 (1988).
Testimony by the alleged indorsee's assistant manager that the promissory note and guaranty were kept in the vault of the indorsee's investor at the indorsee's headquarters established possession and thus status as a holder, even though there was no evidence indicating what relationship the investor and indorsee had with the note. Boyd v. Diversified Financial Systems, 1 S.W.3d 888 (Tex. App. Dallas 1999).

6 §§ 271 to 278.

7 In re Kelton Motors, Inc., 97 F.3d 22, 30 U.C.C. Rep. Serv. 2d 1032 (2d Cir. 1996); In re Investors & Lenders, Ltd., 156 B.R. 145, 21 U.C.C. Rep. Serv. 2d 358 (Bankr. D. N.J. 1993); Troupe v. Redner, 652 So. 2d 394, 25 U.C.C. Rep. Serv. 2d 1303 (Fla. 2d DCA 1995) (decided under the previous version of Article 3).
As to the rights of a holder, generally, see § 232.

8 G.E. Capital Mortg. Services, Inc. v. Neely, 135 N.C. App. 187, 519 S.E.2d 553, 39 U.C.C. Rep. Serv. 2d 1170 (1999).

9 SMS Financial, Ltd. Liability Co. v. ABCO Homes, Inc., 167 F.3d 235, 42 Fed. R. Serv. 3d 1214, 37 U.C.C. Rep. Serv. 2d 1200 (5th Cir. 1999) (whether the Federal Deposit Insurance Corporation reacquired ownership of the promissory note at issue by refunding the purchase price to the plaintiff finance company, which bought the note in a bulk sale, was irrelevant).

End of Document

11 Am. Jur. 2d Bills and Notes § 207

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

A. In General

§ 207. Events giving rise to status as holder of negotiable instrument

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 443

A person can become a holder when an instrument is issued to that person, or the status of holder can arise as the result of an event that occurs after issuance.[1] On the other hand, the delivery of a cashier's check to the remitter who purchased it to pay another party is not a transfer, but the issuance, of the instrument to the remitter, and does not make the remitter either a holder or a nonholder in possession who has the rights of a holder.[2]

If an instrument becomes bearer paper as a result of the manner in which it is indorsed,[3] the person in possession becomes the holder and is entitled to enforce it.[4] However, a transferee of a promissory note is not a holder where the note, an order instrument, has not been indorsed to the transferee, and therefore the transferee may not enforce payment.[5]

The failure of the drawer of a traveler's check to countersign it does not prevent a transferee from becoming a holder of the instrument.[6]

Footnotes

1 U.C.C. § 3-201[Rev] Official Comment 1.

2 Perrino v. Salem, Inc., 243 B.R. 550, 41 U.C.C. Rep. Serv. 2d 566 (D. Me. 1999).

3 § 190.

4 Gerber & Gerber, P.C. v. Regions Bank, 266 Ga. App. 8, 596 S.E.2d 174, 52 U.C.C. Rep. Serv. 2d 815 (2004).
A credit card company was the holder of forged checks, as it was the recipient of instruments indorsed in blank. Getty Petroleum Corp. v. American Exp. Travel Related Services Co., Inc., 90 N.Y.2d 322, 660 N.Y.S.2d 689, 683 N.E.2d 311, 32 U.C.C. Rep. Serv. 2d 1031 (1997).

Where a check made to the order of an escrow agent was indorsed by the agent, thus converting it into bearer paper, and was then given to the plaintiffs, they became holders of the instrument. Nicola v. Burnette, 27 Ohio App. 3d 35, 499 N.E.2d 368, 2 U.C.C. Rep. Serv. 2d 951 (9th Dist. Lorain County 1985).

[5] Carroll v. Kennon, 734 S.W.2d 34, 4 U.C.C. Rep. Serv. 2d 1309 (Tex. App. Waco 1987).

[6] § 82.

End of Document

11 Am. Jur. 2d Bills and Notes § 208

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

A. In General

§ 208. Rights of holder of negotiable instrument not in due course

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 313, 315

While an innocent person who is not a holder in due course may, as transferee, assert the rights of a prior holder in due course,[1] any holder, including one who has not acquired the rights of a holder in due course by transfer and has not qualified as a holder in due course in one's own right, is entitled to enforce an instrument.[2] The rights of a transferee who is not a holder in due course rise no higher than the rights of the transferor.[3] Such a holder not in due course takes an instrument subject to all defenses that would have been available on an action between the original parties.[4] One who is not a holder in due course also takes the instrument subject to all valid claims to it on the part of another indorser.[5] The holder not in due course takes an instrument subject specifically to a claim of a property or possessory right in the instrument or its proceeds, including a claim to rescind a negotiation and to recover the instrument or its proceeds.[6]

Comment:

Claims to which a holder not in due course is subject include not only claims to ownership, but also any other claim of a property or possessory right. It includes the claim to a lien or the claim of a person in rightful possession of an instrument who was wrongfully deprived of possession.[7]

The right, including of a holder not in due course, to enforce the obligation of a party to pay an instrument is subject to the various real defenses.[8] An obligor may further defend an action to enforce an instrument by a holder not in due course by proving that the instrument is a lost or stolen instrument.[9]

Footnotes

1 §§ 224 to 226.

2 § 205.

3 Perry v. Blum, 629 F.3d 1 (1st Cir. 2010) (under Massachusetts law).

4 Resolution Trust Corp. v. Maplewood Investments, 31 F.3d 1276, 24 U.C.C. Rep. Serv. 2d 119 (4th Cir. 1994); Ali, Inc. v. Fishman, 855 F. Supp. 440 (D. Me. 1994); New Haven Savings Bank v. Follins, 431 F. Supp. 2d 183 (D. Mass. 2006); Provident Bank v. MorEquity, Inc., 262 Ga. App. 331, 585 S.E.2d 625, 50 U.C.C. Rep. Serv. 2d 1205 (2003) (could not take clear of perfected security interest); Payne v. Mundaca Inv. Corp., 562 N.E.2d 51 (Ind. Ct. App. 1990); API Supply Co., Inc. v. Premier Bank, 593 So. 2d 660, 17 U.C.C. Rep. Serv. 2d 1185 (La. Ct. App. 1st Cir. 1991), writ denied, 594 So. 2d 896 (La. 1992); Walker v. Probandt, 25 Neb. App. 30, 902 N.W.2d 468, 93 U.C.C. Rep. Serv. 2d 838 (2017), review denied, (May 8, 2018) and cert. denied, 139 S. Ct. 333, 202 L. Ed. 2d 223 (2018); Trueheart v. Braselton, 875 S.W.2d 412, 24 U.C.C. Rep. Serv. 2d 580 (Tex. App. Corpus Christi 1994).
When a negotiable instrument is transferred without indorsement, the assignee takes the note subject to the assignor's equities and defenses available against it. Leavings v. Mills, 175 S.W.3d 301, 54 U.C.C. Rep. Serv. 2d 678 (Tex. App. Houston 1st Dist. 2004).

5 In re Valentine, 146 B.R. 945, 19 U.C.C. Rep. Serv. 2d 174 (Bankr. E.D. Va. 1991).

6 U.C.C. § 3-306[Rev].

7 U.C.C. § 3-306[Rev] Official Comment.

8 U.C.C. § 3-305(a)[Rev], further discussed in § 496.

9 §§ 271 to 278.

End of Document

11 Am. Jur. 2d Bills and Notes § 209

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

A. In General

§ 209. Proof of status as holder of negotiable instrument

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 474, 488, 496(3)

Unless specifically[1] denied in the pleadings, the authenticity of and the authority to make each signature on an instrument is admitted in an action with respect to an instrument.[2] Thus, when a borrower fails to file a sworn pleading contesting the validity of the promissory note on which the plaintiff's action to recover the unpaid balance due is based, the debtor has conclusively admitted the validity of the note and that he or she signed the agreement, and has waived any evidentiary objections thereto.[3]

If the validity of a signature is denied in the pleadings, the burden of establishing validity is on the party claiming validity, but the signature is presumed to be authentic and authorized unless the action is to enforce the liability of the purported signer, and the signer is dead or becomes incompetent at the time of the trial on the issue of the signature's validity.[4] If an action to enforce the instrument is brought against a person as the undisclosed principal of a person who signed the instrument as a party to the instrument, the plaintiff has the burden of establishing that the defendant is liable on the instrument as a represented person under the section of Article 3 governing such transactions.[5]

If the validity of signatures is admitted or proved, a holder producing the instrument is entitled to payment, unless the defendant establishes a defense or a claim of recoupment.[6]

Footnotes

1 U.C.C. § 3-308(a)[Rev].
A debtor's one-sentence general denial of a creditor's petition to enforce a promissory note was not sufficient to constitute a specific denial of the authenticity of her signature, and, therefore, the debtor's signature would be deemed admitted. Wesla Federal Credit Union v. Henderson, 655 So. 2d 691, 28 U.C.C. Rep. Serv. 2d 902 (La. Ct. App. 2d Cir. 1995).

[2] U.C.C. § 3-308(a)[Rev].
A promissory note secured by a real estate mortgage is a "negotiable instrument" under the Uniform Commercial Code (UCC), and therefore is an "instrument" under the U.C.C. provision stating that the authenticity of signatures on instruments are admitted unless specifically denied in the pleadings. Deep Keel, LLC v. Atlantic Private Equity Group, LLC, 413 S.C. 58, 773 S.E.2d 607, 86 U.C.C. Rep. Serv. 2d 937 (Ct. App. 2015).
The purpose of the requirement of a specific denial in the pleadings is to give the plaintiff notice of the defendant's claim of forgery or lack of authority as to the particular signature, and to afford the plaintiff an opportunity to investigate and obtain evidence. U.C.C. § 3-308[Rev] Official Comment 1.

[3] Duchene v. Hernandez, 535 S.W.3d 251 (Tex. App. El Paso 2017).

[4] U.C.C. § 3-308(a)[Rev].

[5] U.C.C. § 3-308(a)[Rev] (citing U.C.C. § 3-402(a)[Rev], discussed in § 440).
The provision regarding undisclosed principals was added to the revised section to take into account U.C.C. § 3-402(a)[Rev] that allows an undisclosed principal to be liable on an instrument signed by an authorized representative and, in such a case, the person enforcing the instrument must prove that the undisclosed principal is liable. U.C.C. § 3-308 Official Comment 1.

[6] U.C.C. § 3-308(b)[Rev].
The mere production of a note entitles the holder to recover unless the maker establishes a defense; and where the maker did not present any evidence to support its contention of a lack of consideration, the holder was entitled to recover. Resolution Trust Corp. v. Juergens, 965 F.2d 149, 18 U.C.C. Rep. Serv. 2d 484 (7th Cir. 1992).

End of Document

11 Am. Jur. 2d Bills and Notes § 210

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

A. In General

§ 210. Rights of transferee of negotiable instrument

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 313

The transfer of an instrument, regardless of whether the transfer is a negotiation, vests in the transferee such rights as the transferor had.[1] Thus, for example, the assignee of promissory note, who acquires the note from the Federal Deposit Insurance Corporation (FDIC), as receiver, inherits the full rights and powers of the original lender through the chain of assignment from the lender to the FDIC to the assignee.[2]

Comment:

The Uniform Commercial Code states that transfer vests in the transferee any right of the transferor to enforce the instrument "including any right as a holder in due course." If the transferee is not a holder because the transferor did not indorse, then the transferee is nevertheless a person entitled to enforce the instrument under Article 3 if the transferor was a holder at the time of the transfer. Although the transferee is not a holder, the transferee has obtained the rights of the transferor as holder. Because the transferee's rights are derivative of the transferor's rights, those rights must be proved. Because the transferee is not a holder, there is no presumption under the Code that the transferee, by producing the instrument, is entitled to payment. The instrument, by its terms, is not payable to the transferee and the transferee must account for possession of the unindorsed instrument by proving the transaction through which the transferee acquired it. Proof of a transfer to the transferee by a holder is proof that the transferee has acquired the rights of a holder.[3]

Footnotes

[1] U.C.C. § 3-203(b)[Rev].
As to acquiring the rights of a holder in due course, see §§ 224 to 226.

[2] Knezovic v. Urban Partnership Bank, 589 B.R. 351 (N.D. Ill. 2018).

[3] U.C.C. § 3-203[Rev] Official Comment 2.

End of Document

11 Am. Jur. 2d Bills and Notes § 211

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

A. In General

§ 211. Rights of transferee of negotiable instrument—To have indorsement

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 313

Forms

Forms relating to complaint to have transferor endorse check, see Am. Jur. Pleading and Practice Forms, Commercial Code [Westlaw®(r) Search Query]

Unless otherwise agreed, if an instrument is transferred for value and the transferee does not become a holder because of a lack of indorsement by the transferor, the transferee has a specifically enforceable right to the unqualified indorsement of the transferor, but negotiation of the instrument does not occur until the indorsement is made.[1]

Comment:

This provision applies only to a transfer for value and only if the instrument is payable to order or is specially indorsed to the transferor.[2] The transferee acquires, in the absence of a contrary agreement, the specifically enforceable right to the indorsement of the transferor. Unless otherwise agreed, it is a right to the general indorsement of the transferor with full liability as indorser, rather than to an indorsement without recourse.[3]

A question may arise if the transferee has paid in advance and the indorsement is omitted fraudulently or through oversight. A transferor who is willing to indorse only without recourse or is unwilling to indorse at all should make those intentions clear before the transfer. The agreement of the transferee to take less than an unqualified indorsement need not be an express one, however, and such an understanding may be implied from conduct, from past practice, or from the circumstances of the transaction.[4]

Footnotes

1 U.C.C. § 3-203(c)[Rev].
As to the negotiation of negotiable instruments by indorsement, see §§ 190 to 204.

2 U.C.C. § 3-203[Rev] Official Comment 3.
As to what constitutes a transfer for value, see §§ 178 to 181.
As to what constitutes an instrument payable to order, see § 187.
As to what constitutes an instrument specially indorsed to the transferor, see § 198.

3 U.C.C. § 3-203[Rev] Official Comment 3.

4 U.C.C. § 3-203[Rev] Official Comment 3.

End of Document

11 Am. Jur. 2d Bills and Notes § 212

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

A. In General

§ 212. Rights of transferee of negotiable instrument—Transferee of partial interest

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 313

If a transferor purports to transfer less than the entire instrument, negotiation of the instrument does not occur.[1] The transferee does not obtains rights under Article 3 and has only the rights of a partial assignee.[2]

Comment:

An indorsement purporting to convey less than the entire instrument does operate as a partial assignment of the cause of action, although Article 3 makes no attempt to state the legal effect of such an assignment, leaving that to other law. On the other hand, an indorsement reading merely "Pay A and B" is effective, since it transfers the entire cause of action to A and B as tenants in common.[3]

Footnotes

1 U.C.C. § 3-203(d)[Rev].

2 U.C.C. § 3-203(d)[Rev].

3 U.C.C. § 3-203[Rev] Official Comment 5.
As to rights to an instrument payable to more than one person, see § 61.

End of Document

11 Am. Jur. 2d Bills and Notes § 213

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

A. In General

§ 213. Title and rights of transferee of nonnegotiable instrument

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 313

Forms

Forms relating to non-negotiable notes, see Am. Jur. Pleading and Practice Forms, Bills and Notes [Westlaw®(r) Search Query]

Article 3, by its terms, applies only to negotiable instruments.[1] Ordinarily, the purchaser of a nonnegotiable instrument is a mere assignee, in the same position as the assignor, whether the purchaser holds by assignment or by indorsement.[2] The transferee receives only such title and rights as the assignor possessed, and ordinarily takes subject to all equities and defenses that would be available between the original parties or could be used against the payee and the assignor,[3] even though the purchaser is given the right to sue in his or her own name.[4] The purchaser, though buying in good faith and for value, acquires only the title of the seller.[5] Thus, since holder-in-due-course status is precluded,[6] all legal or equitable defenses in favor of the makers of the instrument are usually available against any assignee.[7] As in the case of the transfer of a negotiable instrument, the assignment of a nonnegotiable note carries with it the original debt[8] and, as an incident to the transfer, the collateral given for that debt.[9]

Footnotes

1 § 5.

2 Cassetta v. Baima, 106 Cal. App. 196, 288 P. 830 (2d Dist. 1930); People's Sav. Bank of Blakesburg v. Smith, 210

Iowa 136, 230 N.W. 565, 69 A.L.R. 399 (1930); Citizens State Bank v. Pauly, 152 Kan. 152, 102 P.2d 966, 134 A.L.R. 941 (1940); Apple v. Edwards, 92 Mont. 524, 16 P.2d 700, 87 A.L.R. 179 (1932); Persky v. Bank of America Nat. Ass'n, 261 N.Y. 212, 185 N.E. 77 (1933); National City Bank of Cleveland v. Erskine & Sons, 158 Ohio St. 450, 49 Ohio Op. 395, 110 N.E.2d 598 (1953); American Finance Corp. v. Bourne, 1942 OK 61, 190 Okla. 332, 123 P.2d 671 (1942); Janes v. Benson, 155 Pa. 489, 26 A. 752 (1893); Bank of America v. Butterfield, 77 S.D. 170, 88 N.W.2d 909 (1958); Hight v. McCulloch, 150 Tenn. 117, 263 S.W. 794 (1924).

[3] State of Indiana v. Glover, 155 U.S. 513, 15 S. Ct. 186, 39 L. Ed. 243 (1895); In re Metiom, Inc., 301 B.R. 634 (Bankr. S.D. N.Y. 2003); National City Bank of Cleveland v. Erskine & Sons, 158 Ohio St. 450, 49 Ohio Op. 395, 110 N.E.2d 598 (1953).

[4] Farmers' Nat. Bank of Oskaloosa v. Stanton, 191 Iowa 433, 182 N.W. 647, 17 A.L.R. 857 (1921).

[5] Popp v. Exchange Bank, 189 Cal. 296, 208 P. 113 (1922).

[6] § 217.

[7] King v. Harford, 48 Cal. App. 405, 191 P. 998 (1st Dist. 1920).

[8] Knowles v. Sandercock, 107 Cal. 629, 40 P. 1047 (1895).

[9] Seidell v. Tuxedo Land Co., 216 Cal. 165, 13 P.2d 686 (1932).

End of Document

11 Am. Jur. 2d Bills and Notes VII B Refs.

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

Topic Summary | Correlation Table

Research References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 327 to 330, 332 to 334, 336.1, 337, 338.5 to 342, 344, 347.1 to 350, 352.1, 353, 354, 358 to 360, 362, 363
West's Key Number Digest, Finance, Banking, and Credit 997, 1041, 1042

A.L.R. Library

A.L.R. Index, Holder in Due Course
West's A.L.R. Digest, Bills and Notes 327 to 330, 332 to 334, 336.1, 337, 338.5 to 342, 344, 347.1 to 350, 352.1, 353, 354, 358 to 360, 362, 363
West's A.L.R. Digest, Finance, Banking, and Credit 997, 1041, 1042

End of Document

11 Am. Jur. 2d Bills and Notes § 214

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

a. What Constitutes Holder in Due Course

§ 214. What constitutes holder in due course of negotiable instrument, generally

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 327, 329

A.L.R. Library

What constitutes taking instrument in good faith, and without notice of infirmities or defenses, to support holder-in-due-course status, under U.C.C. sec. 3-302, 36 A.L.R.4th 212

Notice which has been forgotten as affecting status as holder in due course, 89 A.L.R.2d 1330

Forms

Forms relating to holder in due course, see Am. Jur. Pleading and Practice Forms, Bills and Notes [Westlaw®(r): Search Query]

Forms relating to holder in due course, generally, see Am. Jur. Pleading and Practice Forms, Commercial Code [Westlaw®(r) Search Query]

A holder in due course is a holder of a negotiable instrument who meets certain qualifications and is thus entitled to enforce an instrument free of most claims or defenses.[1] Subject to the provision on instruments that must carry a statement that they

are subject to claims or defenses,[2] a "holder in due course" means the holder of an instrument[3] if:

(1) the instrument when issued or negotiated to the holder does not bear such apparent evidence of forgery or alteration or is not otherwise so irregular or incomplete as to call into question its authenticity;[4] and
(2) the holder took the instrument for value; in good faith; without notice that the instrument is overdue or has been dishonored or that there is an uncured default with respect to payment of another instrument issued as part of the same series; without notice that the instrument contains an unauthorized signature or has been altered; without notice of any claim to the instrument described in the Code; and without notice that any party has a defense or claim in recoupment described in the Code.[5]

All of the requirements described by the Uniform Commercial Code must be met to qualify as a holder in due course.[6] Check cashing companies may be holders in due course if they meet those requirements with regard to the check at issue.[7]

Observation:

Even though a person may not meet the requirements described above so as to qualify as a holder in due course in his or her own right, that person may assert the rights of a holder in due course under the shelter rule, if the instrument was obtained by way of transfer and a prior party in the chain of transfer was such a holder.[8] On the other hand, certain persons who take outside of the ordinary course are excluded from the definition of a holder in due course.[9]

Footnotes

1 Bricks Unlimited, Inc. v. Agee, 672 F.2d 1255, 33 U.C.C. Rep. Serv. 989 (5th Cir. 1982); Rib Roof Metal Systems, Inc. v. Nat. Storage Centers of Redford, Inc., 68 U.C.C. Rep. Serv. 2d 768 (E.D. Mich. 2009); Aurora Loan Services LLC v. Sadek, 809 F. Supp. 2d 235 (S.D. N.Y. 2011) (under New York law); Erkins v. Alaska Trustee, LLC, 265 P.3d 292 (Alaska 2011); Contrail Leasing Partners, Ltd. v. Executive Service Corp., 100 Nev. 545, 688 P.2d 765, 40 U.C.C. Rep. Serv. 161 (1984); Pascack Community Bank v. Universal Funding, LLP, 419 N.J. Super. 279, 16 A.3d 1097 (App. Div. 2011); Cadle Co., Inc. v. Wallach Concrete, Inc., 1995-NMSC-039, 120 N.M. 56, 897 P.2d 1104, 27 U.C.C. Rep. Serv. 2d 518 (1995); CitiMortgage, Inc. v. Hoge, 196 Ohio App. 3d 40, 2011-Ohio-3839, 962 N.E.2d 327 (8th Dist. Cuyahoga County 2011).
Under the "shelter rule" the transferee of an instrument, notwithstanding a potential defense, nevertheless acquires the rights of the transferor. Pitman Place Development, LLC v. Howard Investments, LLC, 330 S.W.3d 519 (Mo. Ct. App. E.D. 2010).
As to the shelter rule, see §§ 224 to 226.

2 § 216.

3 U.C.C. § 3-302(a)[Rev].
As to what constitutes a holder, generally, see § 206.
As to the necessity that the person be a holder, see § 218.

4 U.C.C. § 3-302(a)(1)[Rev].
As to instruments bearing evidence of forgery or alteration or being otherwise irregular or incomplete, see §§ 235 to 238.

5 U.C.C. § 3-302(a)(2)[Rev].
As to the requirement that the holder took the instrument for value, see §§ 239 to 246.
As to the requirement that the holder took the instrument in good faith, see §§ 247 to 254.
As to the requirement that the holder took the instrument without notice that it contained an unauthorized signature or had been altered, see § 526.

As to the requirement that the holder took the instrument without notice of any claim to it, as defined in U.C.C. § 3-306[Rev], see §§ 255 to 270.

6 Asian Intern., Ltd. v. Merrill Lynch, Pierce, Fenner and Smith, Inc., 435 So. 2d 1058, 37 U.C.C. Rep. Serv. 171 (La. Ct. App. 1st Cir. 1983); American Federal Sav. and Loan Ass'n v. Madison Valley Properties Inc., 1998 MT 93, 288 Mont. 365, 958 P.2d 57, 36 U.C.C. Rep. Serv. 2d 807, 77 A.L.R.5th 729 (1998) (because they are conjunctive); Alliston Hill Trust Co. v. Sarandrea, 236 A.D. 189, 258 N.Y.S. 299 (3d Dep't 1932); Arcanum Nat. Bank v. Hessler, 69 Ohio St. 2d 549, 23 Ohio Op. 3d 468, 433 N.E.2d 204, 33 U.C.C. Rep. Serv. 604 (1982).

7 Triffin v. Somerset Valley Bank, 343 N.J. Super. 73, 777 A.2d 993, 44 U.C.C. Rep. Serv. 2d 1200 (App. Div. 2001).

8 §§ 224 to 226.

9 §§ 227 to 231.

End of Document

11 Am. Jur. 2d Bills and Notes § 215

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

a. What Constitutes Holder in Due Course

§ 215. Policy considerations underlying holder-in-due-course rule

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 327

The basic philosophy of the holder-in-due-course rule is to encourage free negotiability of commercial paper by removing certain defenses against one who takes the paper as an innocent purchaser knowing no reason why the paper is not as sound as indicated on its face.[1]

An important policy objective of Uniform Commercial Code (UCC) provisions on negotiable instruments is to protect the party least able to protect himself or herself; thus, where one of two innocent parties must suffer because of the wrongdoing of a third person, the loss must fall on the party who has by his conduct created the circumstances which enabled the third party to perpetuate the wrong.[2] Since application of the holder-in-due-course provision can result in a loss to an innocent party in favor of a holder in due course,[3] the U.C.C. establishes strict requirements for determining that status, which attempt to identify holders that are worthy (in a commercial sense) of protection, and to separate them from those who are not.[4]

Footnotes

1 Max Duncan Family Investments, Ltd. v. NTFN Inc., 267 S.W.3d 447 (Tex. App. Dallas 2008).

2 Georg v. Metro Fixtures Contractors, Inc., 178 P.3d 1209, 66 U.C.C. Rep. Serv. 2d 477 (Colo. 2008).

3 Georg v. Metro Fixtures Contractors, Inc., 178 P.3d 1209, 66 U.C.C. Rep. Serv. 2d 477 (Colo. 2008).

4 United Catholic Parish Schools of Beaver Dam Educational Ass'n v. Card Services Center, 2001 WI App 229, 248 Wis. 2d 463, 636 N.W.2d 206, 46 U.C.C. Rep. Serv. 2d 754 (Ct. App. 2001).

As to the protection afforded by holder-in-due-course status, see § 232.

End of Document

11 Am. Jur. 2d Bills and Notes § 216

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

a. What Constitutes Holder in Due Course

§ 216. Exception to holder-in-due-course rule for certain consumer transactions

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 328, 329

The section of Article 3 defining what is a holder in due course is subject to the provision on instruments that, under other statutory or administrative law, must carry a statement that they are subject to claims or defenses.[1]

Comment:

There is a large body of state statutory and case law restricting the use of the holder-in-due-course doctrine in consumer transactions, as well as some business transactions that raise similar issues, and this provision subordinates Article 3 to that law and any other similar law.[2]

In addition, in a consumer transaction, if law other than Article 3 requires that an instrument include a statement to the effect that the rights of a holder or transferee are subject to a claim or defense that the issuer could assert against the original payee, and the instrument does not include such a statement, the instrument has the same effect as if the instrument included such a statement, the issuer may assert against the holder or transferee all claims and defenses that would have been available if the instrument included it, and the extent to which claims may be asserted against the holder or transferee is determined as if the instrument included such a statement.[3]

Footnotes

1 U.C.C. § 3-302(a)[Rev], which refers to U.C.C. § 3-106(d)[Rev], discussed in § 83.

2 U.C.C. § 3-302[Rev] Official Comment 7.

3 U.C.C. § 3-305(e)[Rev].

11 Am. Jur. 2d Bills and Notes § 217

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

a. What Constitutes Holder in Due Course

§ 217. Requirement that paper be negotiable for purposes of holder-in-due-course rule

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 327

Since Article 3 of the Uniform Commercial Code applies only to negotiable instruments,[1] for a person to be a holder in due course under Article 3, the instrument must be negotiable.[2] A person who acquires an interest in a document may not be a holder in due course, where the paper was not negotiable for such reasons as it was not payable to owner or bearer,[3] contained a nonrecourse provision[4] or was not for a fixed amount.[5]

Footnotes

1 § 5.

2 Heritage Bank v. Bruha, 283 Neb. 263, 812 N.W.2d 260, 76 U.C.C. Rep. Serv. 2d 836 (2012).
A promissory note did not constitute a negotiable instrument, and thus, the note holder was not subject to the note maker's breach of contract claims against the note's assignor pursuant to the holder-in-due-course statute. Premier Capital, L.L.C. v. Baker, 2012-Ohio-2834, 972 N.E.2d 1125 (Ohio Ct. App. 11th Dist. Portage County 2012).

3 Leavings v. Mills, 175 S.W.3d 301, 54 U.C.C. Rep. Serv. 2d 678 (Tex. App. Houston 1st Dist. 2004) (retail installment contract).

4 Apartment Inv. and Management Co. v. National Loan Investors, L.P., 258 Va. 322, 518 S.E.2d 627 (1999).

5 In re AppOnline.com, Inc., 285 B.R. 805, 49 U.C.C. Rep. Serv. 2d 531 (Bankr. E.D. N.Y. 2002), order aff'd, 321 B.R. 614 (E.D. N.Y. 2003), judgment aff'd, 128 Fed. Appx. 171 (2d Cir. 2004); Barnsley v. Empire Mortg. Ltd. Partnership

V, 142 N.H. 721, 720 A.2d 63, 37 U.C.C. Rep. Serv. 2d 1069 (1998).
Neither the Federal Deposit Insurance Corporation (FDIC), as receiver for a failed bank that had lent money to a borrower, nor an assignee of the FDIC, could become a holder in due course of a promissory note that was not a promise to pay a fixed amount of money and, thus, not a negotiable instrument under the Uniform Commercial Code. Heritage Bank v. Bruha, 283 Neb. 263, 812 N.W.2d 260, 76 U.C.C. Rep. Serv. 2d 836 (2012).
As to the requirements of negotiability, generally, see §§ 36 to 41.
As to the status and rights of a holder of nonnegotiable paper, see § 213.

End of Document

11 Am. Jur. 2d Bills and Notes § 218

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

a. What Constitutes Holder in Due Course

§ 218. Status as holder in due course; necessity of negotiation

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 327, 330

A holder in due course must, among other things,[1] be a holder.[2] Since "holder" is defined as either the person in possession of bearer paper or the person in possession of an instrument payable to an identified person if the person in possession is that identified person,[3] clearly, a person who lacks possession of the instrument cannot be a holder in due course.[4] Furthermore, since negotiation is defined as the transfer of possession of an instrument by a person other than the issuer to a person who thereby becomes a holder,[5] it follows that a person cannot be a holder in due course of an instrument by a transfer that does not amount to a negotiation.[6] Thus, the physical holder of an unendorsed instrument drawn to order is not a holder in due course.[7] When a bank receives a check with a missing indorsement, it does not receive the check by negotiation, and it is not entitled to the rights of a holder in due course, since if a check is transferred with a missing indorsement, no subsequent transferee can become a holder, let alone a holder in due course, unless the missing indorsement is supplied.[8] Similarly, where an indorsement by use of an allonge was invalid, the holder of note has the status of mere transferee rather than of holder in due course.[9]

When the transfer of commercial paper amounts to only an assignment, the transferee is, by definition, not a holder and cannot be a holder in due course.[10]

Footnotes

1 Georg v. Metro Fixtures Contractors, Inc., 178 P.3d 1209, 66 U.C.C. Rep. Serv. 2d 477 (Colo. 2008).

2 U.C.C. § 3-302(a)[Rev].

[3] § 206.

[4] In re Builders Capital and Services, Inc., 317 B.R. 603, 55 U.C.C. Rep. Serv. 2d 447 (Bankr. W.D. N.Y. 2004); River Forest, Inc. v. Multibank 2009-1 RES-ADC Venture, LLC, 331 Ga. App. 435, 771 S.E.2d 126, 86 U.C.C. Rep. Serv. 2d 162 (2015); Western Nat. Bank v. Rives, 927 S.W.2d 681, 33 U.C.C. Rep. Serv. 2d 500 (Tex. App. Amarillo 1996), writ denied, (Feb. 21, 1997).
The purchaser of a promissory note secured by a mortgage was not a holder in due course who could take free and clear of the perfected security interest of the seller's lender, where the purchaser did not have possession of the note when it purchased the mortgage, and when it eventually received possession of the note, it received notice of the security interest at the same time. Provident Bank v. MorEquity, Inc., 262 Ga. App. 331, 585 S.E.2d 625, 50 U.C.C. Rep. Serv. 2d 1205 (2003).

[5] § 185.

[6] In re McMullen Oil Co., 251 B.R. 558, 42 U.C.C. Rep. Serv. 2d 507 (Bankr. C.D. Cal. 2000); In re Dudley, 502 B.R. 259 (Bankr. W.D. Va. 2013) (under Massachusetts law); Creative Ventures, LLC v. Jim Ward & Associates, 195 Cal. App. 4th 1430, 126 Cal. Rptr. 3d 564, 74 U.C.C. Rep. Serv. 2d 641 (6th Dist. 2011); Ederer v. Fisher, 183 So. 2d 39 (Fla. 2d DCA 1965) (holding that the plaintiffs failed to establish the genuine indorsement of the note by the payee to the transferee from whom the plaintiffs purchased the note; therefore, neither the payee's transferee nor plaintiffs acquired the status of holder in due course).
A bank could not become a holder in due course of a draft payable to two payees, where there was lacking the necessary indorsement of one of the payees when the other payee deposited the draft with the bank, there not being a valid negotiation. Federal Deposit Ins. Corp. v. Marine Nat. Bank of Jacksonville, 431 F.2d 341, 7 U.C.C. Rep. Serv. 1327 (5th Cir. 1970).
A purchaser was the holder in due course of promissory notes, despite a claim that he made loans to the payee and did not the purchase the notes, where the holder testified that when he purchased the notes, they were endorsed by the payee, were delivered to him, and he paid a purchase price for them to the payee in installments. Certified Sec. Systems, Inc. v. Yuspeh, 713 So. 2d 558 (La. Ct. App. 4th Cir. 1998).

[7] Big Builders, Inc. v. Israel, 709 A.2d 74 (D.C. 1998).
A bank that took a mortgage on assignment without an indorsement of the mortgage note was not entitled to a claim as holder in due course. Second Nat. Bank of North Miami v. G. M. T. Properties, Inc., 364 So. 2d 59 (Fla. 3d DCA 1978).

[8] In re McMullen Oil Co., 251 B.R. 558, 42 U.C.C. Rep. Serv. 2d 507 (Bankr. C.D. Cal. 2000).

[9] Federal Financial Co. v. Delgado, 1 S.W.3d 181, 40 U.C.C. Rep. Serv. 2d 759 (Tex. App. Corpus Christi 1999).

[10] Tallahassee Bank & Trust Co. v. Raines, 125 Ga. App. 263, 187 S.E.2d 320, 10 U.C.C. Rep. Serv. 665 (1972); Ballengee v. New Mexico Federal Sav. and Loan Ass'n, 1990-NMSC-008, 109 N.M. 423, 786 P.2d 37, 11 U.C.C. Rep. Serv. 2d 124 (1990); Hewett v. Marine Midland Bank of Southeastern New York, N. A., 86 A.D.2d 263, 449 N.Y.S.2d 745, 33 U.C.C. Rep. Serv. 1696 (2d Dep't 1982).

End of Document

11 Am. Jur. 2d Bills and Notes § 219

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

a. What Constitutes Holder in Due Course

§ 219. Taking under restrictive indorsement as affecting status as holder in due course

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 330

The presence on an instrument of a restrictive indorsement[1] does not prevent a purchaser of the instrument from becoming a holder in due course of the instrument, unless the purchaser is a converter as defined in Article 3 or has notice or knowledge of a breach of fiduciary duty as stated in that statute.[2]

Footnotes

1 § 200.

2 U.C.C. § 3-206(e)[Rev], referring to U.C.C. § 3-206(c)[Rev], with respect to the conversion of an instrument bearing a restrictive indorsement, and to U.C.C. § 3-206(d)[Rev], with respect to a purchaser's notice or knowledge of a breach of fiduciary duty.
As to a purchaser's notice or knowledge of a breach of fiduciary duty, see § 266.

End of Document

11 Am. Jur. 2d Bills and Notes § 220

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

a. What Constitutes Holder in Due Course

§ 220. Taking under qualified or "without recourse" indorsement as affecting status as holder in due course

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 330

A qualified indorsement, such as without recourse,[1] does not prevent an indorsee from becoming a holder in due course.[2] Moreover, the use of a qualified indorsement does not of itself constitute notice of a defense or claim against the instrument.[3]

Footnotes

1 § 203.

2 Exchange Bank v. Scholz, 49 Cal. App. 2d 232, 121 P.2d 526 (1st Dist. 1942); Ross v. Title Guarantee & Trust Co., 136 Cal. App. 393, 29 P.2d 236 (4th Dist. 1934).

3 Laschinsky v. Margolis, 129 A.D. 529, 114 N.Y.S. 296 (2d Dep't 1908); First Discount Corp. v. Hatcher Auto Sales, 156 Ohio St. 191, 46 Ohio Op. 87, 102 N.E.2d 4 (1951); Johnson v. Way, 27 Ohio St. 374, 1875 WL 181 (1875); Bederman v. Otisville State Bank, 5 Ohio App. 178, 27 Ohio C.D. 165, 1916 WL 830 (5th Dist. Stark County 1916).

End of Document

11 Am. Jur. 2d Bills and Notes § 221

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

a. What Constitutes Holder in Due Course

§ 221. Payee as holder in due course of negotiable instrument

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 338.5

A payee may qualify as a holder in due course,[1] if the payee satisfies the same requirements as to value, good faith, and lack of notice that apply to any other party claiming that status.[2] However, a payee who deals directly with the drawer or maker is not typically entitled to assert the rights of a holder in due course.[3] For instance, a payee is not a holder in due course of a check, as there was no subsequent negotiation of the check by it to an innocent purchaser for good faith, who could then assert a holder-in-due-course defense when the check was dishonored.[4]

Comment:

The payee of an instrument can be a holder in due course, but use of the holder-in-due-course doctrine by the payee of an instrument is not the normal situation; in the typical case the holder in due course is not the payee of the instrument, but rather is an immediate or remote transferee of the payee. The primary importance of the concept of holder in due course is with respect to the assertion of defenses or claims in recoupment and to the assertions of claims to the instrument. While, if the obligor is the only obligor on the check or note, the holder-in-due-course doctrine is irrelevant in determining rights between the obligor and obligee with respect to the instrument, in a small percentage of cases it is appropriate to allow the payee of an instrument to assert rights as a holder in due course, such as where conduct of some third party is the basis of the defense of the issuer of the instrument.[5]

A bank that is the payee of a check is not a holder in due course if the bank delivers funds to a third party who presents the

check, or the bank deposits them into that person's account, without taking precautions to determine the presenter's power to receive them; the bank may not treat the check as bearer paper and blindly disburse the proceeds according to the instructions of any individual who happens to present the check to the bank, and the teller must inquire into the authority of the presenting party to direct the disposition of the funds.[6]

Footnotes

1 Watson Coatings, Inc. v. American Exp. Travel Related Services, Inc., 436 F.3d 1036 (8th Cir. 2006); In re Lee, 408 B.R. 893 (Bankr. C.D. Cal. 2009); Koss Corp. v. American Exp. Co., 233 Ariz. 74, 309 P.3d 898, 81 U.C.C. Rep. Serv. 2d 603 (Ct. App. Div. 1 2013), as amended, (Sept. 3, 2013); Georg v. Metro Fixtures Contractors, Inc., 178 P.3d 1209, 66 U.C.C. Rep. Serv. 2d 477 (Colo. 2008); Florian v. Lenge, 91 Conn. App. 268, 880 A.2d 985, 58 U.C.C. Rep. Serv. 2d 898 (2005) (payee in possession of note); Exchange Nat. Bank of Winter Haven v. Beshara, 236 So. 2d 198, 7 U.C.C. Rep. Serv. 1146 (Fla. 2d DCA 1970); New Bedford Inst. for Sav. v. Gildroy, 36 Mass. App. Ct. 647, 634 N.E.2d 920, 25 U.C.C. Rep. Serv. 2d 450 (1994); Saale v. Interstate Steel Co., 27 A.D.2d 1, 275 N.Y.S.2d 532, 3 U.C.C. Rep. Serv. 1140 (1st Dep't 1966), order aff'd, 19 N.Y.2d 933, 281 N.Y.S.2d 340, 228 N.E.2d 397, 4 U.C.C. Rep. Serv. 1053 (1967).

2 U.S. v. Second Nat. Bank of North Miami, 502 F.2d 535, 15 U.C.C. Rep. Serv. 870 (5th Cir. 1974); Travelers Cas. and Sur. Co. of America v. Wells Fargo Bank N.A., 374 F.3d 521, 53 U.C.C. Rep. Serv. 2d 695 (7th Cir. 2004) (good faith); Watson Coatings, Inc. v. American Exp. Travel Related Services, Inc., 436 F.3d 1036 (8th Cir. 2006); Gentner and Co. v. Wells Fargo Bank, 76 Cal. App. 4th 1165, 90 Cal. Rptr. 2d 904, 40 U.C.C. Rep. Serv. 2d 38 (2d Dist. 1999); Georg v. Metro Fixtures Contractors, Inc., 178 P.3d 1209, 66 U.C.C. Rep. Serv. 2d 477 (Colo. 2008); Exchange Nat. Bank of Winter Haven v. Beshara, 236 So. 2d 198, 7 U.C.C. Rep. Serv. 1146 (Fla. 2d DCA 1970); Stebbins v. Georgia Power Co., 252 Ga. App. 261, 555 S.E.2d 906, 45 U.C.C. Rep. Serv. 2d 1118 (2001); McIntyre v. Harris, 304 Ill. App. 3d 304, 237 Ill. Dec. 513, 709 N.E.2d 982, 39 U.C.C. Rep. Serv. 2d 200 (3d Dist. 1999).
As to the basic requirements to qualify as a holder in due course, see § 214.

3 Flatiron Linen, Inc. v. First American State Bank, 1 P.3d 244, 39 U.C.C. Rep. Serv. 2d 488 (Colo. App. 1999), as modified on denial of reh'g, (Oct. 21, 1999) and rev'd on other grounds, 23 P.3d 1209, 44 U.C.C. Rep. Serv. 2d 673 (Colo. 2001).

4 Jacobs v. Yates, 342 Ark. 243, 27 S.W.3d 734 (2000).

5 U.C.C. § 3-302[Rev] Official Comment 4 (providing examples).

6 Travelers Cas. and Sur. Co. of America v. Wells Fargo Bank N.A., 374 F.3d 521, 53 U.C.C. Rep. Serv. 2d 695 (7th Cir. 2004); Govoni & Sons Const. Co., Inc. v. Mechanics Bank, 51 Mass. App. Ct. 35, 742 N.E.2d 1094, 43 U.C.C. Rep. Serv. 2d 1058 (2001) (the bank also was on notice of the drawer's claim); Dalton & Marberry, P.C. v. NationsBank, N.A., 982 S.W.2d 231, 37 U.C.C. Rep. Serv. 2d 1 (Mo. 1998); Richards v. Seattle Metropolitan Credit Union, 117 Wash. App. 30, 68 P.3d 1109, 50 U.C.C. Rep. Serv. 2d 499 (Div. 1 2003), as amended (May 30, 2003).
As to notice that the employee's signature was not authorized, see § 264.
As to this providing notice that the employee was acting in breach of fiduciary duty, see § 266.

End of Document

11 Am. Jur. 2d Bills and Notes § 222

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

a. What Constitutes Holder in Due Course

§ 222. Purchaser of limited or partial interest as holder in due course of negotiable instrument

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 330

The purchaser of a limited interest in an instrument, such as a pledgee in a security transaction, can be a holder in due course only to the extent of the interest purchased.[1]

The purchaser of certain payments on real estate lien note was a holder in due course, rather than partial assignee, where the original payee indorsed the note to the purchaser without recourse, the agreement for the first 60 payments under the note gave the purchaser the sole power to enforce the note, and the indorsement did not split the note's ownership.[2]

Footnotes

1 Audsley v. Allen, 774 S.W.2d 142, 10 U.C.C. Rep. Serv. 2d 413 (Mo. 1989).
As to the rights of a person that only holds a security interest in the instrument, see § 233.

2 First Nat. Acceptance Co. v. Dixon, 154 S.W.3d 218 (Tex. App. Beaumont 2004).

End of Document

11 Am. Jur. 2d Bills and Notes § 223

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

a. What Constitutes Holder in Due Course

§ 223. Proof of holder-in-due-course status

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 327

Forms

Forms relating to holder in due course, see Am. Jur. Pleading and Practice Forms, Bills and Notes [Westlaw®(r): Search Query]

Forms relating to holder in due course, generally, see Am. Jur. Pleading and Practice Forms, Commercial Code [Westlaw®(r) Search Query]

Certain claims and defenses are not available to the extent a plaintiff proves that her or she has rights of a holder in due course.[1] Claiming holder-in-due-course status is by nature an estoppel defense, in the sense that if a defense against paying a promissory note is proved, the plaintiff may negate it by proving that the plaintiff is a holder in due course.[2] The party claiming that it is a holder in due course has the burden to establish that status,[3] by proving that taking the instrument was for value, in good faith, and without notice that it is overdue or has been dishonored or of any defense against or claim to it on the part of any person.[4]

Comment:

If a defense or claim in recoupment is proved, the plaintiff may seek to cut off the defense or claim in recoupment by proving that

the plaintiff is a holder in due course, or that the plaintiff has the rights of a holder in due course under the shelter rule. All elements related to the plaintiff's status as a holder in due course under the Code must be proved.[5]

The question whether a holder of a note is a holder in due course becomes one of fact to be determined by the trier of the facts if clearly put in issue.[6]

Possession by the bearer of a note indorsed in blank imports prima facie that the bearer acquired the note in good faith for value and in the course of business, before maturity and without notice of any circumstance impeaching its validity, as required for holder-in-due-course status, and based on the provision on what constitutes sufficient proof of entitlement to payment,[7] the production of the note establishes the bearer's case prima facie against the makers, and such a plaintiff may rest there.[8]

Footnotes

1 U.C.C. § 3-308(b)[Rev].
The effect of holder-in-due-course status on defenses is further discussed in § 495.

2 Jackson v. Mundaca Financial Services, Inc., 349 Ark. 84, 76 S.W.3d 819 (2002).

3 Seinfeld v. Commercial Bank & Trust Co., 405 So. 2d 1039, 32 U.C.C. Rep. Serv. 1137 (Fla. 3d DCA 1981).

4 SKW Real Estate Ltd. Partnership v. Gallicchio, 49 Conn. App. 563, 716 A.2d 903 (1998).

5 U.C.C. § 3-308[Rev] Official Comment 2.
As to a party acquiring the rights of a holder in due course by a transfer of an instrument, see §§ 224 to 226.

6 Vernon v. Yanks, 303 So. 2d 375 (Fla. 3d DCA 1974) (the trial judge, sitting as the trier of the facts, determined that the plaintiff was a holder in due course, and the appellate court declined to disturb this determination on appeal).
The question whether the holder of a note is a holder in due course becomes one of fact to be determined by the trier of the facts if clearly put in issue, and where the pleadings and depositions clearly put in issue whether the holder is a holder in due course, summary judgment for the holder must be reversed. A. B. G. Inv., Inc. v. Selden, 336 So. 2d 444 (Fla. 4th DCA 1976).

7 § 209.

8 SKW Real Estate Ltd. Partnership v. Gallicchio, 49 Conn. App. 563, 716 A.2d 903 (1998).

End of Document

11 Am. Jur. 2d Bills and Notes § 224

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

b. Transferee from Holder in Due Course

§ 224. Shelter rule with respect to transferee from holder in due course of negotiable instrument

Topic Summary | Correlation Table | References

West's Key Number Digest
West's Key Number Digest, Bills and Notes 362

Under the so-called "shelter" rule, the transferee of an instrument, notwithstanding a potential defense, nevertheless acquires the rights of the transferor.[1] More specifically, a transfer of an instrument, whether or not the transfer is a negotiation, vests in the transferee any right of the transferor to enforce the instrument, including any right as holder in due course, but the transferee does not acquire rights of a holder in due course by a transfer, directly or indirectly, from a holder in due course if the transferee engaged in fraud or illegality affecting the instrument.[2]

Under the shelter rule, a transferee obtains the rights, not the status, of the prior holder in due course, and therefore, a holder with notice of defenses is permitted to acquire the rights of a holder in due course.[3] The fact that the possessor of notes is not the holder because they are payable to order and were not indorsed to the possessor does not prevent the possessor from having the rights of a holder in due course, if the possessor's transferor had those rights, but the possessor has the burden of proving that.[4]

Footnotes

1 Pitman Place Development, LLC v. Howard Investments, LLC, 330 S.W.3d 519 (Mo. Ct. App. E.D. 2010).

2 U.C.C. § 3-203(b)[Rev].
A purported assignee of a check issued by the Maryland Child Support Enforcement Administration was a holder in due course of the check under the shelter rule, where the assignee was assigned the check by the check cashing

business at which the payee cashed the check. Triffin v. Maryland Child Support Enforcement Admin., 436 N.J. Super. 621, 95 A.3d 807 (Law Div. 2014).
As to the rights of transferees, generally, see § 210.
The fraud or illegality exception is further discussed in § 225.

[3] Lodge v. United Homes, LLC, 787 F. Supp. 2d 247 (E.D. N.Y. 2011) (under New York law).

[4] Northside Bldg. & Inv. Co. v. Finance Co. of America, 119 Ga. App. 131, 166 S.E.2d 608, 6 U.C.C. Rep. Serv. 345 (1969).

End of Document

11 Am. Jur. 2d Bills and Notes § 225

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

b. Transferee from Holder in Due Course

§ 225. Exception, for fraud or illegality, to shelter rule with respect to transferee from holder in due course of negotiable instrument

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 362

A transferee cannot acquire rights of a holder in due course by a transfer, directly or indirectly, from a holder in due course if the transferee engaged in fraud or illegality affecting the instrument.[1]

Comment:

The application of the exception to the shelter provision is illustrated by the following example: Payee, by fraud, induced Maker to issue a note to Payee. Under the Code, the fraud is a defense to the obligation of Maker to pay the note. Payee negotiated the note to X who took as a holder in due course. Payee then repurchased the note from X. Payee does not succeed to X's rights as a holder in due course and is subject to Maker's defense of fraud.[2]

A situation of the type described above was presented where a bank indorsed notes executed by the limited partners to the partnership and pledged to the bank as collateral to the partnership, and then, acting as the partnership's agent, indorsed the notes back to itself with knowledge of defenses to the notes, including the fact that the partnership had defrauded the limited partners.[3] Similarly, a corporation that procured a cashier's check by fraud was not a holder in due course, even though the check was transferred back to the corporation by a holder in due course.[4] On the other hand, a surety's rights as the transferee

of a promissory note were not affected by the payee's negotiation of the note to a holder in due course, or by an alleged misrepresentation in a "private placement memorandum," which should have been issued to the note's makers concerning the ultimate holder of the note, where the makers knew that their note would be assigned to a possible holder in due course, since the makers never actually received the memorandum, and thus they could not have relied on any alleged misrepresentation in it; the surety was therefore not "a party to any fraud or illegality" by reason of the assignment of the note to a holder in due course and was entitled to the rights of a transferee, unless, as the prior holder, it had notice of a defense or claim against the note.[5]

Footnotes

1 U.C.C. § 3-203(b)[Rev].
A bank was a successor to the holder of a mortgage note and had the same rights as the original holder to name a party to enforce its collection rights; under the shelter principle, the bank acquired all the rights of the previous holder in due course when the mortgage note was transferred to it, even though the note was not properly indorsed, in the absence of evidence that anyone in the chain of title had engaged in fraud or illegality. Anderson v. Burson, 196 Md. App. 457, 9 A.3d 870, 73 U.C.C. Rep. Serv. 2d 207 (2010), judgment aff'd, 424 Md. 232, 35 A.3d 452, 76 U.C.C. Rep. Serv. 2d 255 (2011).

2 U.C.C. § 3-203[Rev] Official Comment 4.

3 Manufacturers Hanover Trust Co. v. Robinson, 157 Misc. 2d 651, 597 N.Y.S.2d 986, 20 U.C.C. Rep. Serv. 2d 993 (Sup 1993).

4 MidAmerica Bank, FSB v. Charter One Bank, FSB, 383 Ill. App. 3d 243, 321 Ill. Dec. 627, 889 N.E.2d 1187, 65 U.C.C. Rep. Serv. 2d 890 (2d Dist. 2008), judgment rev'd on other grounds, 232 Ill. 2d 560, 329 Ill. Dec. 1, 905 N.E.2d 839, 68 U.C.C. Rep. Serv. 2d 289 (2009).

5 National Union Fire Ins. Co. of Pittsburgh, Pa. v. Woodhead, 917 F.2d 752, 12 U.C.C. Rep. Serv. 2d 1076 (2d Cir. 1990).

11 Am. Jur. 2d Bills and Notes § 226

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

b. Transferee from Holder in Due Course

§ 226. Nature of assignment required for party to qualify as holder in due course of negotiable instrument under shelter rule

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 362

A valid assignment of the instruments is required for a party to possess holder-in-due-course status under the shelter rule, such as in the case of a purchaser from a check cashing business, which itself was a holder in due course.[1] It is not necessary for such a purchaser to take the checks by indorsement, where the assignment agreement provides that all payments the purchaser may receive will be the purchaser's exclusive property.[2] Therefore, while a check cashing company could not, by indorsement after the checks were dishonored, confer holder-in-due-course status on a subsequent transferee,[3] it may assign its claim against the drawer of the check to the purchaser, and the purchaser need only prove that the check casher was a holder in due course at the time it paid on the instrument and its assignment to the purchaser was valid.[4]

Footnotes

1 Triffin v. Automatic Data Processing, Inc., 394 N.J. Super. 237, 926 A.2d 362 (App. Div. 2007).

2 Triffin v. Somerset Valley Bank, 343 N.J. Super. 73, 777 A.2d 993, 44 U.C.C. Rep. Serv. 2d 1200 (App. Div. 2001).

3 § 260.

4 Triffin v. Quality Urban Housing Partners, 352 N.J. Super. 538, 800 A.2d 905, 48 U.C.C. Rep. Serv. 2d 651 (App. Div. 2002).

End of Document

11 Am. Jur. 2d Bills and Notes § 227

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

c. Transfers Not Conferring Status as Holder in Due Course of Negotiable Instrument; Federal Holder-in-Due-Course Doctrine

§ 227. Transfers not conferring status as holder in due course of negotiable instrument, generally

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 330

Except to the extent a transferor or predecessor in interest has rights as a holder in due course,[1] a person does not acquire the rights of a holder in due course of an instrument taken by legal process or by purchase in an execution, bankruptcy, or creditor's sale or similar proceeding, by purchase as part of a bulk transaction not in the ordinary course of the transferor's business, or as the successor in interest to an estate or other organization.[2]

Comment:

The Uniform Commercial Code provision is intended to state existing case law. It covers a few situations in which the purchaser takes an instrument under unusual circumstances. The purchaser is treated as a successor in interest to the prior holder and can acquire no better rights. However, if the prior holder was a holder in due course, the purchaser obtains the rights of a holder in due course.[3]

Footnotes

[1] § 224.

[2] U.C.C. § 3-302(c)[Rev].

[3] U.C.C. § 3-302[Rev] Official Comment 5.

End of Document

11 Am. Jur. 2d Bills and Notes § 228

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

c. Transfers Not Conferring Status as Holder in Due Course of Negotiable Instrument; Federal Holder-in-Due-Course Doctrine

§ 228. Transfers by operation of law as conferring status as holder in due course of negotiable instrument

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 330

Forms

Forms relating to holder in due course, see Am. Jur. Pleading and Practice Forms, Bills and Notes [Westlaw®(r): Search Query]

Forms relating to holder in due course, generally, see Am. Jur. Pleading and Practice Forms, Commercial Code [Westlaw®(r) Search Query]

It is a well-settled rule, reflected in the Uniform Commercial Code,[1] that transfers by operation of law, such as those that ensue under the bankruptcy laws, insolvency laws, or laws pertaining to receiverships, are not in the usual course of business, and no better title is acquired by the transferee than that claimed by the previous holders.[2] Accordingly, it is the general rule that a receiver, trustee in bankruptcy, or assignee for the benefit of creditors does not take as a holder in due course so as to preclude defenses that could be asserted against the person whom the fiduciary succeeds, and a purchaser at a receiver's sale takes subject to all defenses and is not a holder in due course.[3]

Comment:

This exception under the Uniform Commercial Code applies to a purchaser at an execution sale or a sale in bankruptcy. It applies equally to an attaching creditor or any other person who acquires the instrument by legal process, or to a representative, such as executor, administrator, receiver or assignee for the benefit of creditors, who takes the instrument as part of an estate. In the absence of controlling state law to the contrary, the exception applies to a sale by a state bank commissioner of the assets of an insolvent bank. However, the statute may be preempted by federal law, if the Federal Deposit Insurance Corporation takes over an insolvent bank. Under the governing federal law, the FDIC and similar financial institution insurers are given holder-in-due-course status and that status is also acquired by their assignees under the shelter doctrine.[4]

A holder in due course does not lose that status by reacquiring title to a negotiable instrument through the judicial sale process, as long as the holder has not lost the right to that status in the interim.[5]

Footnotes

1 U.C.C. § 3-302(c)[Rev], described in § 227.

2 In re Cochise College Park, Inc., 703 F.2d 1339 (9th Cir. 1983); Young v. Victory, 112 Fla. 66, 150 So. 624 (1933); Holly v. Dayton View Terrace Imp. Corp., 25 Ohio Misc. 57, 53 Ohio Op. 2d 393, 54 Ohio Op. 2d 58, 263 N.E.2d 337 (C.P. 1970); Miller v. Diversified Loan Service Co., 181 W. Va. 320, 382 S.E.2d 514 (1989).

3 In re Cochise College Park, Inc., 703 F.2d 1339 (9th Cir. 1983); Young v. Victory, 112 Fla. 66, 150 So. 624 (1933); Holly v. Dayton View Terrace Imp. Corp., 25 Ohio Misc. 57, 53 Ohio Op. 2d 393, 54 Ohio Op. 2d 58, 263 N.E.2d 337 (C.P. 1970); Miller v. Diversified Loan Service Co., 181 W. Va. 320, 382 S.E.2d 514 (1989).
A stranger to the paper cannot become a holder in due course by purchasing at a judicial sale. Finance Co. of America v. Wilson, 115 Ga. App. 280, 154 S.E.2d 459, 4 U.C.C. Rep. Serv. 312 (1967).
A person who buys a promissory note at an execution sale is not a holder in due course, but acquires a title that is subject to the personal defenses that could have been asserted against the payee. Boswell v. Reid, 199 Cal. App. 2d 705, 19 Cal. Rptr. 29 (3d Dist. 1962).

4 U.C.C. § 3-302[Rev] Official Comment 5.
As to the doctrines applicable to instruments acquired by the FDIC and similar federal agencies, see § 231.

5 Finance Co. of America v. Wilson, 115 Ga. App. 280, 154 S.E.2d 459, 4 U.C.C. Rep. Serv. 312 (1967).

End of Document

11 Am. Jur. 2d Bills and Notes § 229

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

c. Transfers Not Conferring Status as Holder in Due Course of Negotiable Instrument; Federal Holder-in-Due-Course Doctrine

§ 229. Succession in interest of estate or organization as conferring status as holder in due course of negotiable instrument

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 330

Forms

Forms relating to holder in due course, see Am. Jur. Pleading and Practice Forms, Bills and Notes [Westlaw®(r): Search Query]

Forms relating to holder in due course, generally, see Am. Jur. Pleading and Practice Forms, Commercial Code [Westlaw®(r) Search Query]

A person does not acquire rights of a holder in due course of an instrument taken as the successor in interest to an estate or other organization.[1] For instance, after a bank that is not a holder in due course is absorbed by another bank as a result of a merger, the successor bank is also not a holder in due course.[2]

Comment:

This exception would apply to a new partnership taking over for value all of the assets of an old one after a new member has entered the firm or to a reorganized or consolidated corporation taking over the assets of a predecessor.[3]

Footnotes

[1] U.C.C. § 3-302(c)[Rev].
A successor corporation, which continues the business, takes over the assets, and retains many of the officers of the original corporation, is not a holder in due course of paper transferred by the original corporation. Hawthorn-Mellody, Inc. v. Driessen, 213 Kan. 791, 518 P.2d 446 (1974).

[2] Carolina First Nat. Bank v. Douglas Gallery of Homes, Ltd., 68 N.C. App. 246, 314 S.E.2d 801 (1984).

[3] U.C.C. § 3-302[Rev] Official Comment 5.
As to the bulk purchase exception also possibly being applicable, see § 230.

End of Document

11 Am. Jur. 2d Bills and Notes § 230

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

c. Transfers Not Conferring Status as Holder in Due Course of Negotiable Instrument; Federal Holder-in-Due-Course Doctrine

§ 230. Bulk purchase as conferring status as holder in due course of negotiable instrument

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 330

A person does not acquire the rights of a holder in due course of an instrument taken by purchase as part of a bulk transaction not in the ordinary course of business of the transferor.[1] This rule applies to situations where a new business organization takes over, for value, the assets of an old one.[2] The provision operates regarding those bulk transfers incident to the cessation, liquidation, or reorganization of the transferor's business, where the circumstances indicate that the transferee is a mere successor in interest to the transferor.[3]

Comment:

This provision also applies to the purchase by one bank of a substantial part of the paper held by another bank that is threatened with insolvency and seeking to liquidate its assets. In the absence of controlling state law to the contrary, this provision also applies to a sale by a state bank commissioner of the assets of an insolvent bank, unless preempted by federal law.[4]

Where there has been a bulk transfer incident to the liquidation of a going enterprise or a transfer of a business of which the negotiable instruments represent part of the assets transferred, the transferee acquires no more protected interest than the transferor had.[5] On the other hand, where there is a substantial transfer as a matter of the regular commercial dealings of an ongoing business, the transferee is not put on notice that the paper transferred is not fully and freely negotiable, and, in the

absence of any notice of the transferor's insolvency, the transferee is a holder in due course.[6] Therefore, a purchaser of an instrument as part of a bulk transaction may become a holder in due course unless the transaction was not in the regular course of the transferor's business,[7] and the Code does not bar holder-in-due-course status where there is no evidence that in making the bulk transfer, the transferor was acting outside of the ordinary course of its business.[8] A factual issue may be presented, where the maker asserts that the payee was not a financial institution regularly engaged in the business of selling notes at a discount,[9] and the person suing on the instrument has the burden of establishing that the transaction was in the regular course of the transferor's business.[10]

Taking a note as security for a loan is not "purchase" within the meaning of the statute denying status as a holder in due course of a note taken by purchase as part of a bulk transaction.[11] A transferee who acquires a single note from a liquidating trust does not take the note as part of a bulk transaction so as to preclude it from being a holder in due course.[12]

Footnotes

1 U.C.C. § 3-302(c)(ii)[Rev].
A bulk transferee cannot be a holder in due course. P P Inc. v. McGuire, 509 F. Supp. 1079, 31 Fed. R. Serv. 2d 379, 31 U.C.C. Rep. Serv. 606 (D.N.J. 1981).

2 First Nat. Bank of Tribune, Kan. v. Lohman, 827 P.2d 583, 16 U.C.C. Rep. Serv. 2d 1098 (Colo. App. 1992).

3 First Alabama Bank of Guntersville v. Hunt, 402 So. 2d 992, 31 U.C.C. Rep. Serv. 151 (Ala. Civ. App. 1981), writ denied, 402 So. 2d 995 (Ala. 1981).
As to the succession exception also possibly being applicable, see § 229.

4 U.C.C. § 3-302[Rev] Official Comment 5.
As to the federal holder-in-due-course doctrine, see § 231.

5 Pugatch v. David's Jewelers, 53 Misc. 2d 327, 278 N.Y.S.2d 759, 4 U.C.C. Rep. Serv. 202 (N.Y. City Civ. Ct. 1967).

6 Pugatch v. David's Jewelers, 53 Misc. 2d 327, 278 N.Y.S.2d 759, 4 U.C.C. Rep. Serv. 202 (N.Y. City Civ. Ct. 1967).

7 Ginsburg v. Cadle Co., 61 Conn. App. 388, 764 A.2d 210 (2001).

8 Northwestern Nat. Ins. Co. v. Maggio, 976 F.2d 320, 18 U.C.C. Rep. Serv. 2d 808 (7th Cir. 1992).

9 Combine Intern. v. Berkley, 141 A.D.2d 465, 529 N.Y.S.2d 790, 8 U.C.C. Rep. Serv. 2d 64 (1st Dep't 1988).

10 Credit Industrial Corp. v. DiNanno, 5 U.C.C. Rep. Serv. 877 (Mass. App. Div. 1964).

11 Groner v. Regency Federal Sav. and Loan Ass'n, 248 Ill. App. 3d 574, 188 Ill. Dec. 64, 618 N.E.2d 634, 23 U.C.C. Rep. Serv. 2d 127 (1st Dist. 1993).

12 First Nat. Bank of Tribune, Kan. v. Lohman, 827 P.2d 583, 16 U.C.C. Rep. Serv. 2d 1098 (Colo. App. 1992).

11 Am. Jur. 2d Bills and Notes § 231

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

c. Transfers Not Conferring Status as Holder in Due Course of Negotiable Instrument; Federal Holder-in-Due-Course Doctrine

§ 231. Federal holder-in-due-course doctrine and *D'Oench, Duhme* doctrine

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Finance, Banking, and Credit 997, 1041, 1042

It has been noted that the Federal Deposit Insurance Corporation (FDIC)generally cannot qualify as a holder in due course of notes acquired in a purchase and assumption transaction from a failed bank, because it does not technically qualify as a holder under the Uniform Commercial Code's definition of that term, and because it often acquires those notes through bulk transactions.[1] However, precluding the FDIC and other government receivers and their assignees or transferees from having the rights of a holder in due course would hamper their statutory function of resolving bank failures. To avoid this result, the so-called "federal holder-in-due-course doctrine" has arisen. This doctrine affords federal bank regulatory agencies the same defenses accorded a holder in due course under state law, even where those agencies do not meet the state law requirements for status as a holder in due course.[2] Under that doctrine, a subsequent holder who acquires notes from the FDIC may also be afforded special status as a holder in due course, as long as the note is properly negotiated to it.[3] To preserve the resale market for notes acquired by the FDIC from a failed bank, the federal holder-in-due-course doctrine affords one who purchases notes from the FDIC special status as a holder in due course, even though the requirements of state law are not technically met.[4] However, the special protection of the federal holder-in-due-course doctrine is afforded only when necessary to further the policy of promoting the stability of the nation's banking system by facilitating the FDIC's smooth acquisition of bank assets.[5]

The federal holder-in-due-course doctrine, including its application to assignees from bank regulatory agencies, is not available if the paper was not negotiable.[6] As a precondition to the ability to claim holder-in-due-course status, the note must have been properly negotiated to the purchaser by the FDIC—which means that if the note is specially indorsed, it must carry the further indorsement of the person indicated; thus, where a note acquired from a failed bank was indorsed with the words "Pay to the order of the Federal Reserve Bank" but the FDIC never obtained the indorsement of the Federal Reserve Bank prior to transferring the note to the purchaser, the purchaser was not a holder in due course.[7]

Observation:

Closely related to the federal holder-in-due-course doctrine is the *D'Oench, Duhme* doctrine, which protects the Federal Deposit Insurance Corporation from personal defenses on notes that are not evidenced by an examination of the books and records of the failed bank.[8] In effect, the doctrine confers holder-in-due-course status on the FDIC.[9]

Footnotes

1 Cadle Co., Inc. v. Wallach Concrete, Inc., 1995-NMSC-039, 120 N.M. 56, 897 P.2d 1104, 27 U.C.C. Rep. Serv. 2d 518 (1995).

2 Resolution Trust Corp. v. Kennelly, 57 F.3d 819 (9th Cir. 1995); Cadle Co., Inc. v. Wallach Concrete, Inc., 1995-NMSC-039, 120 N.M. 56, 897 P.2d 1104, 27 U.C.C. Rep. Serv. 2d 518 (1995).

3 Cadle Co., Inc. v. Wallach Concrete, Inc., 1995-NMSC-039, 120 N.M. 56, 897 P.2d 1104, 27 U.C.C. Rep. Serv. 2d 518 (1995); Alma Group, L.L.C. v. Palmer, 143 S.W.3d 840 (Tex. App. Corpus Christi 2004).

4 Johnson v. Drury, 763 So. 2d 103 (La. Ct. App. 5th Cir. 2000); Cadle Co., Inc. v. Wallach Concrete, Inc., 1995-NMSC-039, 120 N.M. 56, 897 P.2d 1104, 27 U.C.C. Rep. Serv. 2d 518 (1995); Bosque Asset Corp. v. Greenberg, 19 S.W.3d 514 (Tex. App. Eastland 2000).

5 Cadle Co., Inc. v. Wallach Concrete, Inc., 1995-NMSC-039, 120 N.M. 56, 897 P.2d 1104, 27 U.C.C. Rep. Serv. 2d 518 (1995) (further holding that the federal holder-in-due-course doctrine did not apply where the defense was based on the FDIC's own conduct allegedly breaching an implied promise to the guarantor on the note to liquidate the collateral before taking action under the guaranty agreement).

6 Federal Sav. and Loan Ins. Corp. v. Mackie, 962 F.2d 1144 (5th Cir. 1992); Resolution Trust Corp. v. Montross, 944 F.2d 227, 15 U.C.C. Rep. Serv. 2d 1249 (5th Cir. 1991); Apartment Inv. and Management Co. v. National Loan Investors, L.P., 258 Va. 322, 518 S.E.2d 627 (1999) (promissory note that contained a non-recourse provision).

7 Cadle Co., Inc. v. Wallach Concrete, Inc., 1995-NMSC-039, 120 N.M. 56, 897 P.2d 1104, 27 U.C.C. Rep. Serv. 2d 518 (1995).

8 D'Oench, Duhme & Co. v. Federal Deposit Ins. Corporation, 315 U.S. 447, 62 S. Ct. 676, 86 L. Ed. 956 (1942); Federal Sav. and Loan Ins. Corp. v. Cribbs, 918 F.2d 557, 13 U.C.C. Rep. Serv. 2d 797 (5th Cir. 1990); Sunbelt Sav., FSB, Dallas, Texas v. Amrecorp Realty Corp., 742 F. Supp. 370, 13 U.C.C. Rep. Serv. 2d 176 (N.D. Tex. 1990).
For a general discussion of the *D'Oench, Duhme* doctrine, see Am. Jur. 2d, Banks and Financial Institutions §§ 1059 to 1065.

9 Am. Jur. 2d, Banks and Financial Institutions § 1059.

End of Document

11 Am. Jur. 2d Bills and Notes § 232

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

d. Rights of Holder in Due Course

§ 232. Nature of title and protection accorded to holder in due course of negotiable instrument

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 327, 363

The holder-in-due-course concept is an exception to the common-law rule that a purchaser can acquire no better title than the transferor had,[1] and a holder in due course may obtain better rights than its predecessor had.[2] With certain limited exceptions,[3] a person having the rights of a holder in due course takes free of a claim to the instrument.[4] That is, holder in due course status gives the holder of an instrument such as a check the right to enforce it and to cut off certain defenses of the obligor under the instrument.[5] A holder in due course is insulated from nearly all claims of any party,[6] including common-law claims for money had and received and unjust enrichment.[7] The right of a holder in due course to enforce the obligation of a party to pay an instrument, like the right of a holder not in due course, is subject to the real defenses, but it is not subject personal ones.[8]

A holder in due course holds a title that is valid against all the world. The protection accorded a holder in due course operates to cut off equities and personal defenses. Pursuant to the policy of freedom of negotiability, courts are averse to the adoption of rules that would place on a holder in due course a burden that would unduly hamper the transferability of the negotiable paper, and are inclined to adopt and support rules and doctrines that bolster the position of a holder in due course.[9]

Footnotes

1 Swiss Air Transport Co., Ltd. v. Benn, 121 Misc. 2d 129, 467 N.Y.S.2d 341, 37 U.C.C. Rep. Serv. 404 (N.Y. City Civ. Ct. 1983), judgment rev'd on other grounds, 128 Misc. 2d 657, 494 N.Y.S.2d 781 (App. Term 1985).

2 Fine v. Sovereign Bank, 671 F. Supp. 2d 219 (D. Mass. 2009) (under Massachusetts law); In re McMullen Oil Co.,

251 B.R. 558, 42 U.C.C. Rep. Serv. 2d 507 (Bankr. C.D. Cal. 2000).

[3] City Rentals, Inc. v. Kesler, 191 Ohio App. 3d 474, 2010-Ohio-6264, 946 N.E.2d 785 (3d Dist. Defiance County 2010).
Exceptions to the rule are discussed in §§ 235 to 270.

[4] U.C.C. § 3-306[Rev].
A holder in due course takes an instrument free of all claims to the instrument and of all defenses of any party to the instrument with whom the holder has not dealt. IFC Credit Corp. v. Specialty Optical Systems, Inc., 252 S.W.3d 761 (Tex. App. Dallas 2008).
As to the assertion of a claim of a property or possessory right in an instrument against a holder not in due course, see § 208.

[5] Jenkins v. Wachovia Bank, Nat. Ass'n, 309 Ga. App. 562, 711 S.E.2d 80, 74 U.C.C. Rep. Serv. 2d 478 (2011).

[6] United Catholic Parish Schools of Beaver Dam Educational Ass'n v. Card Services Center, 2001 WI App 229, 248 Wis. 2d 463, 636 N.W.2d 206, 46 U.C.C. Rep. Serv. 2d 754 (Ct. App. 2001).

[7] Watson Coatings, Inc. v. American Exp. Travel Related Services, Inc., 436 F.3d 1036 (8th Cir. 2006).
An defendant in an action for money had and received, based on allegations that checks received by the defendant were actually due to the plaintiff, was protected by its holder-in-due-course status. Fedeli v. UAP/Ga. Ag. Chem., Inc., 237 Ga. App. 337, 514 S.E.2d 684, 38 U.C.C. Rep. Serv. 2d 845 (1999).

[8] § 496.

[9] Valley Bank & Trust Co. v. American Utilities, Inc., 415 F. Supp. 298, 19 U.C.C. Rep. Serv. 857 (E.D. Pa. 1976); American Bank of the South v. Rothenberg, 598 So. 2d 289 (Fla. 5th DCA 1992); Contrail Leasing Partners, Ltd. v. Executive Service Corp., 100 Nev. 545, 688 P.2d 765, 40 U.C.C. Rep. Serv. 161 (1984); First Nat. Bank of Andrews v. Jones, 635 S.W.2d 950 (Tex. App. Eastland 1982), writ refused n.r.e.

End of Document

11 Am. Jur. 2d Bills and Notes § 233

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

d. Rights of Holder in Due Course

§ 233. Rights of holder with security interest in instrument

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 363

If the person entitled to enforce an instrument has only a security interest in the instrument, and the person obliged to pay the instrument has a defense, claim in recoupment, or claim to the instrument that may be asserted against the person who granted the security interest, the person entitled to enforce the instrument may assert rights as a holder in due course only to an amount payable under the instrument that, at the time of the enforcement of the instrument, does not exceed the amount of the unpaid obligation secured.[1]

Comment:

Under this provision, if, for example, a payee negotiates a note of a maker for $1,000 to a holder as security for payment of the payee's debt to the holder of $600, the holder may assert rights as a holder in due course only to the extent of $600; with respect to $400 of the note, the maker may assert any rights that the maker has against the payee.[2]

Footnotes

[1] U.C.C. § 3-302(e)[Rev].

[2] U.C.C. § 3-302[Rev] Official Comment 6.

End of Document

11 Am. Jur. 2d Bills and Notes § 234

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

1. In General

d. Rights of Holder in Due Course

§ 234. Rights of holder of instrument given for promise of performance that has been partially performed

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 363

If the promise of performance that is the consideration for an instrument has been partially performed, the holder may assert rights as a holder in due course of the instrument only to the fraction of the amount payable under the instrument equal to the value of the partial performance divided by the value of the promised performance.[1]

Comment:

This provision was added at the time of the revision of Article 3 to clarify a matter not specifically addressed in the former Article 3, and would apply, for example, where a payee negotiates a $1,000 note to a holder who agrees to pay $900 for it. After paying $500, the holder learns that the payee defrauded the maker in the transaction giving rise to the note. Under this provision, the holder may assert rights as a holder in due course to the extent of $555.55 ($500 divided by $900 and then multiplied by $1,000). This formula rewards the holder with a ratable portion of the bargained-for profit.[2]

Footnotes

[1] U.C.C. § 3-302(d)[Rev].
As to giving value to the extent a promise of performance has been performed, see § 242.

[2] U.C.C. § 3-302[Rev] Official Comment 6.
As to value being given even though an instrument is purchased for less than its face amount, see § 246.

End of Document

11 Am. Jur. 2d Bills and Notes § 235

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

2. Instruments Bearing Apparent Evidence Calling into Question Authenticity

§ 235. Holder-in-due-course rule as applied to instruments bearing apparent evidence calling into question authenticity, generally

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 342

Forms

Forms relating to holder-in-due-course and irregular, forgery, alteration, of instrument, generally, see Am. Jur. Pleading and Practice Forms, Commercial Code [Westlaw®(r) Search Query]

A holder may qualify as a holder in due course if the instrument when issued or negotiated to the holder does not bear such apparent evidence of forgery or alteration or is not otherwise so irregular or incomplete as to call into question its authenticity.[1]

Comment:

The revised version of Article 3 represents a return to the rule that the taker of an irregular or incomplete instrument is not a person the law should protect against defenses of the obligor or claims of prior owners. This reflects a policy choice against extending the holder-in-due-course doctrine to an instrument that is so incomplete or irregular "as to call into question its authenticity." The term "authenticity" is used to make it clear that the irregularity or incompleteness must indicate that the instrument may not be what it purports to be. Persons who purchase or pay for such instruments should do so at their own risk. Under the corresponding section of the prior version, irregularity or incompleteness gave a purchaser notice of a claim or defense, but it was not clear from that provision whether the claim or defense had to be related to the irregularity or incomplete aspect of

the instrument. That ambiguity is not present in the revised statute.[2]

Moreover, a holder may qualify as a holder in due course notwithstanding irregularities with a check, including misspellings in the name of the payee, which call its authenticity into question, where the holder investigates the irregularities in a commercially reasonable manner by calling the payor to verify the check, and the drawee bank to confirm that sufficient funds exist to pay the check.[3]

Footnotes

1 U.C.C. § 3-302(a)(1)[Rev].
As to instruments bearing apparent evidence of incompleteness, see § 237.
As to circumstances indicating that instruments bear apparent evidence of irregularity, see § 238.

2 U.C.C. § 3-302[Rev] Official Comment 1.

3 New Randolph Halsted Currency Exchange, Inc. v. Regent Title Ins. Agency, LLC, 405 Ill. App. 3d 923, 345 Ill. Dec. 844, 939 N.E.2d 1024, 73 U.C.C. Rep. Serv. 2d 341 (1st Dist. 2010).

End of Document

11 Am. Jur. 2d Bills and Notes § 236

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

2. Instruments Bearing Apparent Evidence Calling into Question Authenticity

§ 236. Holder-in-due-course rule as applied to instruments showing signs of alteration

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 342

Forms

Forms relating to alteration, see Am. Jur. Pleading and Practice Forms, Bills and Notes [Westlaw®(r): Search Query]

If a reasonable inspection of the instrument would disclose a material alteration in its terms, and the appearance of the alteration indicates that it was probably made by someone other than the original drafter, the instrument is not regular on its face, and one who takes it in that condition does not have the rights of a holder in due course. The extent of the alteration is not so important as its obviousness.[1] Thus, the mere fact that a holder knows that a blank has been filled in does not bar holder-in-due-course status, even where the holder personally filled in a blank for the payee's name pursuant to a letter of instructions accompanying the instrument.[2]

Footnotes

1 New Rochelle Securities Co. v. International Thrift Society, 270 N.Y. 52, 200 N.E. 71 (1936).
As to the duty to make inquiry, see § 249.

2 Riggs Nat. Bank of Washington, D. C. v. Dade Federal Sav. and Loan Ass'n of Miami, 268 F.2d 951 (5th Cir. 1959).
As to the effect of completing an incomplete instrument, see §§ 99 to 102.

End of Document

11 Am. Jur. 2d Bills and Notes § 237

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

2. Instruments Bearing Apparent Evidence Calling into Question Authenticity

§ 237. Incompleteness of negotiable instrument as affecting applicability of holder-in-due-course rule

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 342

An instrument is not complete and regular on its face, and there cannot be a holder in due course of it, where, at the time of taking, the instrument contained blanks or omissions rendering it incomplete.[1] This is the case where an instrument is signed in blank, or there is an omission or blank as to amount payable, the name of the payee, or the time of payment or due date.[2] Thus, a bank could not be a holder in due course of a check that was not complete and regular on its face.[3] However, the mere fact that there is an omission in an instrument does not preclude holder-in-due-course status, if the omission is not material enough to make the instrument incomplete.[4] Also, the fact that a check was drawn on a customer's draft form and had an unfilled blank space for the payee did not create a danger signal so as to require one acquiring it for value to investigate whether the drawer's name was forged.[5]

Footnotes

1 Wilkins v. Reliance Equipment Co., 259 Ala. 348, 67 So. 2d 16 (1953).

2 Atkinson v. Englewood State Bank, 141 Colo. 436, 348 P.2d 702 (1960).

3 Goff v. Morgan County Nat. Bank, 144 Fla. 671, 198 So. 484 (1940).

4 Atkinson v. Englewood State Bank, 141 Colo. 436, 348 P.2d 702 (1960); SFC Acceptance Corp. v. Spain, 251 La. 902, 207 So. 2d 364 (1968) (the schedule of payment section was left blank in a note attached to the bottom of a sale and chattel mortgage instrument).

5 Riggs Nat. Bank of Washington, D. C. v. Dade Federal Sav. and Loan Ass'n of Miami, 268 F.2d 951 (5th Cir. 1959).

As to the effect of completing an incomplete instrument, see §§ 99 to 102.

End of Document

11 Am. Jur. 2d Bills and Notes § 238

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

2. Instruments Bearing Apparent Evidence Calling into Question Authenticity

§ 238. Miscellaneous circumstances indicating irregularity of negotiable instrument as affecting holder-in-due-course rule

Topic Summary | Correlation Table | References

West's Key Number Digest
West's Key Number Digest, Bills and Notes 342

Banks that cash checks are not holders in due course if they fail to exercise ordinary care to determine whether the checks were forged or otherwise deficient, under such circumstances as that the account holder at the bank who presented the checks was not a party to any of the checks, the checks contained multiple endorsements, which all appeared to be in the same handwriting, and the checks were all marked "for deposit only."[1] A bank was on notice of potential foul play, and could not qualify as holder in due course, when an employee of a corporate drawer that was not itself indebted to bank presented a check that was drawn to the bank's order and attempted to obtain payment on it, since the check itself posed the unanswered question concerning whom the bank was to pay.[2] Similarly, check cashing companies are not holders in due course, if they cashed stolen money orders with telltale unmatching serial numbers and disregarded a warning on the instruments that they would not be paid if stolen, providing a toll free number where information concerning their authenticity could be obtained,[3] or where the check casher made no effort to verify a postdated check's validity.[4]

A payee's knowledge that a customer was presenting checks that had the facsimile signatures of the customer's employer, the bookkeeper was a fiduciary, and the funds were for customer's personal benefit called the checks' authenticity into question, and thus that they were irregular, and the payee was not a holder in due course.[5]

The facts that some of the papers are dated one day after other papers, and that some have typed entries and others have handwritten entries, do not constitute such "irregularity" as to constitute notice of any matter that would bar a taker from being a holder in due course.[6] While indications on a note of partial payments made on the date of the note by persons not parties to the note may be somewhat unusual, they do not necessarily make the note other than complete and regular on its face, so as to prevent a holder from qualifying as a holder in due course.[7]

Footnotes

1 Firstar Bank, N.A. v. First Service Title Agency, Inc., 2004-Ohio-4509, 54 U.C.C. Rep. Serv. 2d 701 (Ohio Ct. App. 1st Dist. Hamilton County 2004).

2 Mutual Service Cas. Ins. Co. v. Elizabeth State Bank, 265 F.3d 601, 45 U.C.C. Rep. Serv. 2d 281 (7th Cir. 2001).

3 Triffin v. Travelers Express Co., Inc., 370 N.J. Super. 399, 851 A.2d 667, 53 U.C.C. Rep. Serv. 2d 934 (App. Div. 2004).

4 Buckeye Check Cashing, Inc. v. Camp, 159 Ohio App. 3d 784, 2005-Ohio-926, 825 N.E.2d 644, 56 U.C.C. Rep. Serv. 2d 484 (2d Dist. Greene County 2005).

5 Willowglen Academy-Wisconsin, Inc. v. Connelly Interiors, Inc., 2008 WI App 35, 307 Wis. 2d 776, 746 N.W.2d 570, 64 U.C.C. Rep. Serv. 2d 1062 (Ct. App. 2008).

6 Indemnity Ins. Co. of North America v. American Deseret Ltd. Partnership, 887 F. Supp. 521 (S.D. N.Y. 1993), judgment aff'd, 56 F.3d 460 (2d Cir. 1995).

7 Riggs Nat. Bank of Washington, D. C. v. Dade Federal Sav. and Loan Ass'n of Miami, 268 F.2d 951 (5th Cir. 1959).

End of Document

11 Am. Jur. 2d Bills and Notes § 239

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

3. Taking Instrument for Value

§ 239. Taking instrument for value, for purposes of holder-in-due-course rule, generally

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 352.1

A.L.R. Library

When is instrument issued or transferred for "value" under U.C.C. s 3-303, 77 A.L.R.5th 429

To be a holder in due course of a negotiable instrument, the holder must have taken the instrument for value.[1]

A holder obtained a promissory note for value, even though it could not specify the amount it paid for the note, because the note was purchased along with a number of others.[2]

Observation:

Under the shelter provision, a person who has not given value for an instrument, and who therefore does not qualify as a holder in due course, may have the rights of a holder in due course acquired from a predecessor in interest.[3]

Footnotes

[1] U.C.C. § 3-302(a)(2)(i)[Rev].
A real estate brokerage company, acting as escrow agent, which accepted the tender of a deposit check from a prospective purchaser, did not qualify as a holder in due course, because it did not take the instrument for value. Liebowitz v. Wright Properties, Inc., 427 So. 2d 783, 35 U.C.C. Rep. Serv. 862 (Fla. 4th DCA 1983).

[2] Cadle Co. v. Ginsburg, 51 Conn. App. 392, 721 A.2d 1246, 37 U.C.C. Rep. Serv. 2d 684 (1998).

[3] §§ 224 to 226.

End of Document

11 Am. Jur. 2d Bills and Notes § 240

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

3. Taking Instrument for Value

§ 240. What constitutes value for purposes of holder-in-due-course rule, generally

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 352.1, 353

A.L.R. Library

When is instrument issued or transferred for "value" under U.C.C. s 3-303, 77 A.L.R.5th 429

An instrument is issued or transferred for value if:
(1) the instrument is issued or transferred for a promise of performance, to the extent the promise has been performed;[1]
(2) the transferee acquires a security interest or other lien in the instrument other than a lien obtained by judicial proceeding;[2]
(3) the instrument is issued or transferred as payment of, or as security for, an antecedent claim against any person, whether or not the claim is due;[3]

(4) the instrument is issued or transferred in exchange for a negotiable instrument;[4] or
(5) the instrument is issued or transferred in exchange for the incurring of an irrevocable obligation to a third party by the person taking the instrument.[5]

Comment:

The definition of value has primary importance in cases in which the issue is whether the holder of an instrument is a holder in due course, and particularly in cases in which the issuer of the instrument has a defense to the instrument. Suppose Buyer and Seller signed a contract on April 1 for the sale of goods to be delivered on May 1. Payment of 50% of the price of the goods was due on

signing the contract. On April 1, Buyer delivered to Seller a check in the amount due under the contract. The check was drawn by X to Buyer as payee and was indorsed to Seller. When the check was presented for payment to the drawee on April 2, it was dishonored because X had stopped payment. At that time, Seller had not taken any action to perform the contract with Buyer. If X has a defense on the check, the defense can be asserted against Seller who is not a holder in due course because Seller did not give value for the check. The policy basis for this provision is that the holder who gives an executory promise of performance will not suffer an out-of-pocket loss to the extent the executory promise is not performed at the time the holder learns of dishonor of the instrument. When Seller took delivery of the check on April 1, Buyer's obligation to pay 50% of the price on the date was suspended, but when the check was dishonored on April 2 the obligation revived. If payment for goods is due at or before delivery and the buyer fails to make the payment, the seller is excused from performing the promise to deliver the goods. Thus, Seller is protected from an out-of-pocket loss even if the check is not enforceable. Holder-in-due-course status is not necessary to protect Seller.[6]

Footnotes

1 U.C.C. § 3-303(a)(1)[Rev], further discussed in § 242.

2 U.C.C. § 3-303(a)(2)[Rev], further discussed in § 243.

3 U.C.C. § 3-303(a)(3)[Rev], further discussed in § 244.

4 U.C.C. § 3-303(a)(4)[Rev], further discussed in § 245.

5 U.C.C. § 3-303(a)(5)[Rev], further discussed in § 245.

6 U.C.C. § 3-303[Rev] Official Comment 2.
U.C.C. § 3-303[Rev] Official Comment 1 provides various other examples.

11 Am. Jur. 2d Bills and Notes § 241

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

3. Taking Instrument for Value

§ 241. Distinction between “value” and “consideration” for purposes of holder-in-due-course rule

Topic Summary | Correlation Table | References

West’s Key Number Digest
West’s Key Number Digest, Bills and Notes 352.1

The term “consideration” is defined in Article 3 as any consideration sufficient to support a simple contract.[1] If an instrument is issued for value, it is also issued for consideration.[2]

Comment:

The distinction between value and consideration in Article 3 is a very fine one. Whether an instrument is taken for value is relevant to the issue of whether a holder is a holder in due course. If an instrument is not issued for consideration, the issuer has a defense to the obligation to pay the instrument.[3] The definition of value in Article 1,[4] which includes any consideration sufficient to support a simple contract, does not apply to Article 3. Thus, outside Article 3, anything that is consideration is also value. A different rule applies in Article 3, which states that if an instrument is issued for value it is also issued for consideration.[5]

Value includes purchasing a note on the secondary market for valuable consideration.[6]

Footnotes

1 U.C.C. § 3-303(b)[Rev].

2 U.C.C. § 3-303(b)[Rev].

3 U.C.C. § 3-303[Rev] Official Comment 1.

4 Now contained in U.C.C. § 1-204[Rev].

5 U.C.C. § 3-303[Rev] Official Comment 1.

6 In re AppOnline.Com, Inc., 290 B.R. 1, 49 U.C.C. Rep. Serv. 2d 1241 (Bankr. E.D. N.Y. 2003).

End of Document

11 Am. Jur. 2d Bills and Notes § 242

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

3. Taking Instrument for Value

§ 242. Promise of performance as value for purposes of holder-in-due-course rule

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 352.1, 353

A.L.R. Library

When is instrument issued or transferred for "value" under U.C.C. s 3-303, 77 A.L.R.5th 429

An instrument is issued or transferred for value if the instrument is issued or transferred for a promise of performance, to the extent the promise has been performed.[1] This is in accord with the view that an executory promise is not "value."[2] For instance, a client received value for endorsing checks to a law firm as payment for the retainer, as an element of the firm's claim to be a holder in due course, only to the extent that the law firm had actually performed legal services for the client before it acquired the checks.[3]

Footnotes

[1] U.C.C. § 3-303(a)(1)[Rev].
Attorneys who acquired a note as payment for services performed by them for the payee could be holders in due course only to the extent of the amount of the value of services performed; in the absence of evidence of the value of those services, summary judgment for the attorneys was error. Fernandez v. Cunningham, 268 So. 2d 166, 11 U.C.C. Rep. Serv. 805 (Fla. 3d DCA 1972).
Even if the parties effectively agreed that a creditor would discharge a note and release a lien on the collateral in exchange for payment of the debt, U.C.C. § 3-303(a)(1)[Rev] would be applicable where the creditor was in the

process of performing its end of that bargain when it was notified by a bank that the cashier's check used to pay the debt was purchased with stolen funds, and the creditor would be a holder in due course only to the extent that it had actually performed; i.e., to the extent that it had actually discharged the note and released the lien. American Federal Sav. and Loan Ass'n v. Madison Valley Properties Inc., 1998 MT 93, 288 Mont. 365, 958 P.2d 57, 36 U.C.C. Rep. Serv. 2d 807, 77 A.L.R.5th 729 (1998).

[2] Carter & Grimsley v. Omni Trading, Inc., 306 Ill. App. 3d 1127, 240 Ill. Dec. 187, 716 N.E.2d 320, 39 U.C.C. Rep. Serv. 2d 484 (3d Dist. 1999).

[3] Carter & Grimsley v. Omni Trading, Inc., 306 Ill. App. 3d 1127, 240 Ill. Dec. 187, 716 N.E.2d 320, 39 U.C.C. Rep. Serv. 2d 484 (3d Dist. 1999).
As to the monetary extent to which the holder may assert rights as a holder in due course in this situation, see § 234.

End of Document

11 Am. Jur. 2d Bills and Notes § 243

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

3. Taking Instrument for Value

§ 243. Acquiring security interest in or lien on instrument as value for purposes of holder-in-due-course rule

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 352.1, 353

A.L.R. Library

When is instrument issued or transferred for "value" under U.C.C. s 3-303, 77 A.L.R.5th 429

An instrument is issued or transferred for value if the transferee acquires a security interest or other lien in the instrument, other than a lien obtained in a judicial proceeding.[1]

Comment:

The Uniform Commercial Code equates value with the obtaining of a security interest or nonjudicial lien in the instrument. The term "security interest" covers Article 9 cases in which an instrument is taken as collateral, as well as bank collection cases in which a bank acquires a security interest under Article 4. The acquisition of a common-law or statutory banker's lien is also value under the Code. An attaching creditor or other person who acquires a lien by judicial proceedings does not give value for the purposes of Article 3.[2]

Footnotes

[1] U.C.C. § 3-303(a)(2)[Rev].
Security interests are discussed in Am. Jur. 2d, Secured Transactions §§ 1 et seq.

[2] U.C.C. § 3-303[Rev] Official Comment 3, referring to the lien granted a bank in a collection item under U.C.C. § 4-210[Rev], discussed in Am. Jur. 2d, Banks and Financial Institutions §§ 842 to 847.

End of Document

11 Am. Jur. 2d Bills and Notes § 244

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

3. Taking Instrument for Value

§ 244. Taking instrument for antecedent claim as value for purposes of holder-in-due-course rule

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 358, 359

A.L.R. Library

When is instrument issued or transferred for "value" under U.C.C. s 3-303, 77 A.L.R.5th 429

Forms

Forms relating to existing indebtedness or antecedent debt, see Am. Jur. Pleading and Practice Forms, Commercial Code [Westlaw®(r) Search Query]

An instrument is issued or transferred for value if the instrument is issued or transferred as payment of, or as security for, an antecedent claim against any person, regardless of whether the claim is due.[1] This provision creates a presumption that consideration exists in such an exchange and places the burden on the maker to overcome that presumption.[2] However, the payee must irrevocably change its position before being given notice of a defect in a check to have taken it for value, and merely marking a loan "paid" is not sufficient until the satisfaction documents are placed in the mail, and administrative steps taken to treat the debt as paid are irreversible.[3]

The rule that value includes taking an instrument in payment of an antecedent claim encompasses situations where those claims were purchased by the person who later received the check at issue in payment of them.[4] A lender that took checks in payment on the borrower's outstanding debt takes them for value, as required for holder-in-due-course status.[5] A bank's application of the proceeds of a deposited negotiable instrument to the depositor's antecedent debt owed to the bank is the giving of value for the instrument and makes the bank a holder in due course.[6] Likewise, a utility company that provided services and takes a check in the ordinary course of business without notice of the irregularity, and applies the amount of the check to the customer's account, is a holder in due course.[7]

Comment:

The rule that an instrument taken for an antecedent debt is taken for value applies even though there is no extension of time or other concession, and regardless of whether the claim is due. The rule also applies to any claim against any person; there is no requirement that the claim arise out of a contract. In particular, the provision is intended to apply to an instrument given in payment of or as security for the debt of a third person, even though a concession is not made in return.[8]

Footnotes

1 U.C.C. § 3-303(a)(3)[Rev].

2 Sverdrup Corp. v. Politis, 888 S.W.2d 753, 25 U.C.C. Rep. Serv. 2d 857 (Mo. Ct. App. E.D. 1994).

3 American Federal Sav. and Loan Ass'n v. Madison Valley Properties Inc., 1998 MT 93, 288 Mont. 365, 958 P.2d 57, 36 U.C.C. Rep. Serv. 2d 807, 77 A.L.R.5th 729 (1998) (noting that after the creditor received notice that a cashier's check used to pay the debt was purchased with stolen funds, the creditor wrote "stamped in error" next to the "paid" stamp on the note, and retrieved the lien release papers from its outgoing mail basket, thereby indicating that by the time the creditor had received notice, it still had the capability to reverse the steps indicating that the loan had been paid).

4 In re Joe Morgan, Inc., 985 F.2d 1554, 20 U.C.C. Rep. Serv. 2d 401 (11th Cir. 1993) (factor that purchased receivables at a 5% discount of the face value of each account gave value for the checks it subsequently collected from account debtors).
An investor who was assigned a mortgage by an investment corporation in payment of a claim against an affiliate company was a holder in due course of the promissory note that was executed with the mortgage, where the note was taken for value; even though the investment preceded the note, the assignee took the note in payment of her claim against a bankrupt mortgage corporation arising from her investment, and, therefore, she took the note for value, since it was in payment of an antecedent claim. Thomas v. State Mortg., Inc., 176 Mich. App. 157, 439 N.W.2d 299, 9 U.C.C. Rep. Serv. 2d 1276 (1989).

5 Fedeli v. UAP/Ga. Ag. Chem., Inc., 237 Ga. App. 337, 514 S.E.2d 684, 38 U.C.C. Rep. Serv. 2d 845 (1999).

6 Exchange Nat. Bank of Winter Haven v. Beshara, 236 So. 2d 198, 7 U.C.C. Rep. Serv. 1146 (Fla. 2d DCA 1970).

7 Stebbins v. Georgia Power Co., 252 Ga. App. 261, 555 S.E.2d 906, 45 U.C.C. Rep. Serv. 2d 1118 (2001).

8 U.C.C. § 3-303[Rev] Official Comment 4.

11 Am. Jur. 2d Bills and Notes § 245

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

3. Taking Instrument for Value

§ 245. Exchange of instrument for other instrument or for irrevocable obligation to third party as value for purposes of holder-in-due-course rule

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 353, 360

A.L.R. Library

When is instrument issued or transferred for "value" under U.C.C. s 3-303, 77 A.L.R.5th 429

An instrument is issued or transferred for value if it is issued or transferred in exchange for a negotiable instrument[1] or if it is issued or transferred in exchange for the incurring of an irrevocable obligation to a third party by the person taking the instrument.[2] For instance, a purchaser took negotiable instruments consisting of United States government payment-in-kind certificates for value, where the purchaser issued its check in exchange for the certificates.[3]

Comment:

These provisions state generally recognized exceptions to the rule that an executory promise is not value. A negotiable instrument is value because it carries the possibility of negotiation to a holder in due course, after which the party who gives it is obligated to pay. The same reasoning applies to any irrevocable commitment to a third person, such as a letter of credit issued when an instrument is taken.[4]

Footnotes

1 U.C.C. § 3-303(a)(4)[Rev].

2 U.C.C. § 3-303(a)(5)[Rev].

3 Allison-Kesley Ag Center, Inc. v. Hildebrand, 485 N.W.2d 841, 19 U.C.C. Rep. Serv. 2d 480 (Iowa 1992).

4 U.C.C. § 3-303[Rev] Official Comment 5.

End of Document

11 Am. Jur. 2d Bills and Notes § 246

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

3. Taking Instrument for Value

§ 246. Value less than amount of instrument for purposes of holder-in-due-course rule

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 354

A.L.R. Library

When is instrument issued or transferred for "value" under U.C.C. s 3-303, 77 A.L.R.5th 429

The payment of the full face value of a draft or note is not necessary to make one a holder for value.[1] One may be a holder for value and in due course, even without paying the full face amount of the instrument, and this fact alone does not preclude recovery of the full amount.[2] This result is based on the view that negotiable paper may be bought and sold like anything else at its real or supposed value, and the transfer of such an instrument at a discount greater than the legal rate of interest does not deprive the transferee of the protection of a bona fide purchaser for value.[3]

Observation:

However, paying substantially less than the face amount or taking an instrument at a large discount is considered on the question whether the holder takes in good faith and without notice so as to qualify as a holder in due course.[4]

Footnotes

1 Sample v. Hundred Lakes Corp., 107 Fla. 568, 145 So. 193 (1933).

2 Szczotka v. Idelson, 228 Cal. App. 2d 399, 39 Cal. Rptr. 466 (2d Dist. 1964).

3 Hunt v. NationsCredit Financial Services Corp., 902 So. 2d 75 (Ala. Civ. App. 2004).

4 § 251.

End of Document

11 Am. Jur. 2d Bills and Notes § 247

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

4. Taking Instrument in Good Faith

§ 247. Taking instrument in good faith, for purposes of holder-in-due-course rule, generally

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 337

A.L.R. Library

What constitutes taking instrument in good faith, and without notice of infirmities or defenses, to support holder-in-due-course status, under U.C.C. sec. 3-302, 36 A.L.R.4th 212

Forms

Forms relating to holder in good faith, see Am. Jur. Pleading and Practice Forms, Commercial Code [Westlaw®(r) Search Query]

To be a holder in due course, a holder must have taken the instrument in good faith.[1]

Observation:

Under the "shelter" doctrine incorporated in Article 3, even if a person taking an instrument does not act in good faith and, therefore, does not qualify as a holder in due course in his or her own right, that person may still have the rights of a holder in due

course if a predecessor in interest qualified as one.[2]

Footnotes

1 U.C.C. § 3-302(a)(2)(ii)[Rev].
Acquisition of the instrument in good faith is an absolutely necessary prerequisite to becoming a holder in due course. McCarthy v. Kasperak, 3 Ohio App. 3d 206, 444 N.E.2d 472, 35 U.C.C. Rep. Serv. 540 (8th Dist. Cuyahoga County 1981).
Questions of fact existed whether a holder took a note in good faith and without notice of certain defenses, and, thus, put in issue the question whether the holder was a holder in due course. A. B. G. Inv., Inc. v. Selden, 336 So. 2d 444 (Fla. 4th DCA 1976).

2 §§ 224 to 226.

11 Am. Jur. 2d Bills and Notes § 248

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

4. Taking Instrument in Good Faith

§ 248. Standard of good faith for purposes of holder-in-due-course rule

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 337

A.L.R. Library

What constitutes taking instrument in good faith, and without notice of infirmities or defenses, to support holder-in-due-course status, under U.C.C. sec. 3-302, 36 A.L.R.4th 212

The phrase "good faith" is defined generally in Article 3 as honesty in fact, as well as the observance of reasonable commercial standards of fair dealing.[1] Honesty in fact is tested by a subjective standard, inquiring into a party's actual state of mind, while observance of reasonable commercial standards of fair dealing requires an objective measurement of the fairness of a party's actions in light of prevailing commercial standards, and both components must be satisfied.[2] Even if a holder complies with commercial standards, those standards must be reasonably related to achieving fair dealing.[3]

Comment:

Failure to exercise ordinary care in conducting a transaction is an entirely different concept than failure to deal fairly in conducting the transaction. Both fair dealing and ordinary care are to be judged in the light of reasonable commercial standards, but those standards in each case are directed to different aspects of commercial conduct.[4]

A holder establishes good faith, as required for holder-in-due-course status, by testifying that one took the instrument in complete innocence and by disclosing the circumstances of the transfer.[5] "Honesty in fact" is defined as the absence of bad faith or dishonesty with respect to a party's conduct within a commercial transaction.[6] However, the holder may not act "with a pure heart and an empty head," but must comport with reasonable commercial standards of fair dealing,[7] and all the circumstances must be considered.[8] "Bad faith" means, in this context, guilty knowledge or willful ignorance.[9] Thus, a holder obtains an instrument in good faith, absent evidence that the holder deliberately failed to make inquiry so as to remain ignorant of facts that it feared would disclose a defect in the transaction, or paid an amount far less than the instrument's face value.[10]

Observation:

The definition of good faith in Article 2 does not apply to Article 3.[11]

Footnotes

1 U.C.C. § 3-103(4)[Rev].

2 Wells Fargo Bank NA v. Ferruggio Insurance Services of LA Incorporated, 358 F. Supp. 3d 887, 97 U.C.C. Rep. Serv. 2d 894 (D. Ariz. 2019); Any Kind Checks Cashed, Inc. v. Talcott, 830 So. 2d 160, 48 U.C.C. Rep. Serv. 2d 800 (Fla. 4th DCA 2002); Maine Family Federal Credit Union v. Sun Life Assur. Co. of Canada, 1999 ME 43, 727 A.2d 335, 37 U.C.C. Rep. Serv. 2d 875 (Me. 1999); Hathorn v. Loftus, 143 N.H. 304, 726 A.2d 1278, 37 U.C.C. Rep. Serv. 2d 676 (1999); Triffin v. Pomerantz Staffing Services, LLC, 370 N.J. Super. 301, 851 A.2d 100, 53 U.C.C. Rep. Serv. 2d 927 (App. Div. 2004); Regent Corp., U.S.A. v. Azmat Bangladesh, Ltd., 253 A.D.2d 134, 686 N.Y.S.2d 24, 38 U.C.C. Rep. Serv. 2d 131 (1st Dep't 1999).

3 Banco Bilbao Vizcaya Argentaria v. Easy Luck Co., Inc., 208 So. 3d 1241, 91 U.C.C. Rep. Serv. 2d 859 (Fla. 3d DCA 2017).

4 U.C.C. § 3-103[Rev] Official Comment 4.

5 Big Builders, Inc. v. Israel, 709 A.2d 74 (D.C. 1998).

6 Buckeye Check Cashing, Inc. v. Camp, 159 Ohio App. 3d 784, 2005-Ohio-926, 825 N.E.2d 644, 56 U.C.C. Rep. Serv. 2d 484 (2d Dist. Greene County 2005).

7 Any Kind Checks Cashed, Inc. v. Talcott, 830 So. 2d 160, 48 U.C.C. Rep. Serv. 2d 800 (Fla. 4th DCA 2002).

8 Any Kind Checks Cashed, Inc. v. Talcott, 830 So. 2d 160, 48 U.C.C. Rep. Serv. 2d 800 (Fla. 4th DCA 2002) (a holder must take a global view of the underlying transaction and all of its participants); Advanta Business Services Corp. v. Five C's Hardware & Paint Store, Inc., 256 A.D.2d 369, 681 N.Y.S.2d 569 (2d Dep't 1998).

9 Georg v. Metro Fixtures Contractors, Inc., 178 P.3d 1209, 66 U.C.C. Rep. Serv. 2d 477 (Colo. 2008).
To obtain negotiable instrument in "bad faith," the purchaser must have acquired the instrument with actual knowledge of its infirmity, or with a belief based on facts or circumstances as known to the purchaser that there was a defense, or acting dishonestly. In re SGE Mortgage Funding Corp., 278 B.R. 653 (Bankr. M.D. Ga. 2001).
Bad faith in the taking of an instrument is not simply bad judgment or negligence; it implies a conscious wrongdoing due to a dishonest purpose or moral obliquity, and may be inferred from unheeded suspicious circumstances of a substantial character, even though the evidence adduced is insufficient of itself to support a finding that the taker had

actual knowledge of the defect. Canfield v. Bank One, Texas, N.A., 51 S.W.3d 828, 45 U.C.C. Rep. Serv. 2d 571 (Tex. App. Texarkana 2001).

[10] Cadle Co. v. Ginsburg, 51 Conn. App. 392, 721 A.2d 1246, 37 U.C.C. Rep. Serv. 2d 684 (1998).
As to the duty of inquiry, see § 249.
As to the effect of purchasing an instrument at less than face value, see § 251.

[11] Choo Choo Tire Service, Inc. v. Union Planters Nat. Bank, 231 Ga. App. 346, 498 S.E.2d 799, 35 U.C.C. Rep. Serv. 2d 924 (1998).

End of Document

11 Am. Jur. 2d Bills and Notes § 249

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

4. Taking Instrument in Good Faith

§ 249. Duty of inquiry for purposes of holder-in-due-course rule

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 339

Protection afforded a holder in due course cannot be used to shield one who refuses to investigate when facts known to him or her suggest an irregularity concerning the commercial paper that the holder takes.[1] A party who fails to make an inquiry, reasonably required by the circumstances of the transaction, so as to remain ignorant of facts that might disclose a defect cannot claim to be a holder of an instrument in due course.[2] However, a duty of inquiry will be implied only if circumstances reveal a deliberate desire by the holder to evade knowledge of a claim by the maker.[3] To constitute bad faith, the person taking the instrument must have had knowledge of such substantial facts and circumstances as to create a suspicion that there was something wrong with the title of the person from whom it was taken, the instrument itself, or the money represented by that instrument, combined with an intentional disregard of and refusal to learn the facts using the means that the taker knows are available.[4] To defeat the rights of one dealing with negotiable securities it is not enough to show that he or she took them under circumstances which ought to excite the suspicion of a prudent person and cause him or her to make inquiry; rather, it must be established that the taker had actual knowledge of an infirmity or defect, or of such facts that the failure to make further inquiry would indicate a deliberate desire on such person's part to evade knowledge because of a belief or fear that investigation would disclose a vice in the transaction.[5] It has also been said that mere negligence or failure to make inquiries which a reasonably prudent person would make does not of itself amount to bad faith on the part of the holder of a negotiable instrument, but if a party fails to make an inquiry for the purpose of remaining ignorant of facts which the party believes or fears would disclose a defect in the transaction, such party may be found to have acted in bad faith.[6]

When an instrument appears regular on its face, the holder should not be under a duty of inquiry, unless, under the circumstances, there are suspicions so cogent and obvious that to remain passive would amount to bad faith.[7] Thus, as a general rule, the holder of a promissory note is not obligated to make any inquiry into the nature of the transaction or the ability of the makers to pay.[8]

Footnotes

1 Stewart v. Thornton, 116 Ariz. 107, 568 P.2d 414, 22 U.C.C. Rep. Serv. 990 (1977); Triffin v. Pomerantz Staffing Services, LLC, 370 N.J. Super. 301, 851 A.2d 100, 53 U.C.C. Rep. Serv. 2d 927 (App. Div. 2004) (a check cashing company that failed to examine checks to determine whether they contained heat sensitive ink as stated on those checks was not a holder in due course, since the ink only required touching to determine whether the checks were authentic).

2 Triffin v. Liccardi Ford, Inc., 417 N.J. Super. 453, 10 A.3d 227, 73 U.C.C. Rep. Serv. 2d 400 (App. Div. 2011).

3 Schwegmann Bank & Trust Co. of Jefferson v. Simmons, 880 F.2d 838, 9 U.C.C. Rep. Serv. 2d 602 (5th Cir. 1989); Mid-Continent Nat. Bank v. Bank of Independence, 523 S.W.2d 569, 16 U.C.C. Rep. Serv. 1286 (Mo. Ct. App. 1975).

4 Canfield v. Bank One, Texas, N.A., 51 S.W.3d 828, 45 U.C.C. Rep. Serv. 2d 571 (Tex. App. Texarkana 2001).

5 New Randolph Halsted Currency Exchange, Inc. v. Regent Title Ins. Agency, LLC, 405 Ill. App. 3d 923, 345 Ill. Dec. 844, 939 N.E.2d 1024, 73 U.C.C. Rep. Serv. 2d 341 (1st Dist. 2010).

6 Community Bank v. Ell, 278 Or. 417, 564 P.2d 685, 21 U.C.C. Rep. Serv. 1349 (1977).
Negligence as related to good faith for purposes of holder-in-due-course rule, generally, see § 250.

7 Hollywood Nat. Bank v. International Business Machines Corp., 38 Cal. App. 3d 607, 113 Cal. Rptr. 494, 14 U.C.C. Rep. Serv. 782 (2d Dist. 1974).

8 National Union Fire Ins. Co. of Pittsburgh, Pa. v. Woodhead, 917 F.2d 752, 12 U.C.C. Rep. Serv. 2d 1076 (2d Cir. 1990) (holder in due course despite lack of knowledge of a purported inconsistency between financial information provided on the makers' subscription application to the payee of the note and financial information reported on the makers' tax return).

End of Document

11 Am. Jur. 2d Bills and Notes § 250

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

4. Taking Instrument in Good Faith

§ 250. Negligence as related to good faith for purposes of holder-in-due-course rule

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 337

The test of a holder's good faith is knowledge of facts, not due care or negligence,[1] and a holder may be accorded holder in due course status where it acts pursuant to reasonable commercial standards of fair dealing, even if it is negligent.[2] Mere negligence or lack of diligence on the part of the purchaser of a negotiable instrument for value and before maturity, with respect to infirmities in the paper or defects in the title to it, will not defeat a holder's title or right of recovery; even gross negligence is not itself sufficient.[3] However, negligence, and particularly gross negligence, may be considered with other circumstances as evidence of bad faith.[4] Bad faith may be presumed from a reckless refusal to inquire.[5] Bad faith sufficient to deny holder-in-due-course status is a conscious state, which can include deliberate avoidance of inquiry by one who fears what inquiry would bring to light.[6]

Observation:

The definition of good faith in revised Article 3 requires not only honesty in fact but also "observance of reasonable commercial standards of fair dealing." Although fair dealing is a broad term that must be defined in context, it is clear that it is concerned with the fairness of conduct rather than the care with which an act is performed. Failure to exercise ordinary care in conducting a transaction is an entirely different concept than failure to deal fairly in conducting the transaction.[7]

Footnotes

1 Barnett Bank of Palm Beach County, N.A. v. Regency Highland Condominium Ass'n, Inc., 452 So. 2d 587, 38 U.C.C. Rep. Serv. 1289 (Fla. 4th DCA 1984); Industrial Nat. Bank of Rhode Island v. Leo's Used Car Exchange, Inc., 362 Mass. 797, 291 N.E.2d 603, 11 U.C.C. Rep. Serv. 917 (1973).

2 Banco Bilbao Vizcaya Argentaria v. Easy Luck Co., Inc., 208 So. 3d 1241, 91 U.C.C. Rep. Serv. 2d 859 (Fla. 3d DCA 2017).

3 Valley Nat. Bank v. Porter, 705 F.2d 1027, 36 U.C.C. Rep. Serv. 207 (8th Cir. 1983); Money Mart Check Cashing Center, Inc. v. Epicycle Corp., 667 P.2d 1372, 36 U.C.C. Rep. Serv. 1255 (Colo. 1983); Industrial Nat. Bank of Rhode Island v. Leo's Used Car Exchange, Inc., 362 Mass. 797, 291 N.E.2d 603, 11 U.C.C. Rep. Serv. 917 (1973); St. Cloud Nat. Bank & Trust Co. v. Sobania Const. Co., Inc., 302 Minn. 71, 224 N.W.2d 746, 15 U.C.C. Rep. Serv. 679 (1974); Canfield v. Bank One, Texas, N.A., 51 S.W.3d 828, 45 U.C.C. Rep. Serv. 2d 571 (Tex. App. Texarkana 2001).

4 Industrial Nat. Bank of Rhode Island v. Leo's Used Car Exchange, Inc., 362 Mass. 797, 291 N.E.2d 603, 11 U.C.C. Rep. Serv. 917 (1973); Canfield v. Bank One, Texas, N.A., 51 S.W.3d 828, 45 U.C.C. Rep. Serv. 2d 571 (Tex. App. Texarkana 2001).

5 Saka v. Sahara-Nevada Corp., 92 Nev. 703, 558 P.2d 535, 20 U.C.C. Rep. Serv. 958 (1976).

6 Northwestern Nat. Ins. Co. v. Maggio, 976 F.2d 320, 18 U.C.C. Rep. Serv. 2d 808 (7th Cir. 1992).

7 § 248.

End of Document

11 Am. Jur. 2d Bills and Notes § 251

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

4. Taking Instrument in Good Faith

§ 251. Taking at discount or purchasing at less than face value as related to good faith for purposes of holder-in-due-course rule

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 337, 354

The mere fact that a note is purchased for an amount less than its face value is not of itself sufficient to charge the purchaser with notice of existing equities, unless the consideration is nominal.[1] A discount of 9%, for example, although large, was not so great under the circumstances as to support an inference that the holder knew that the notes had been dishonestly or improperly acquired.[2] However, the fact that an instrument is discounted or purchased at less than its face value is a circumstance to be considered with all the evidence in determining whether the purchaser acquired the instrument in good faith and without notice.[3] Inadequacy in the amount paid for a note may, with suspicious circumstances, authorize a finding of bad faith, especially if the consideration is grossly inadequate.[4] The fact that a note was offered and purchased at an unusual and unbusinesslike discount, or at a grossly inadequate price, may be sufficient to impose a duty of inquiry on the purchaser, and, taken together with other facts, might bar holder-in-due-course status.[5] Therefore, where a purchaser has an anticipated return representing the equivalent of an annual interest rate of 203%, the extraordinarily favorable terms of the note clearly indicate that this is an unusual type of commercial transaction, and a subsequent purchaser will be denied holder-in-due-course status.[6]

Footnotes

1 Northwestern Nat. Ins. Co. v. Maggio, 976 F.2d 320, 18 U.C.C. Rep. Serv. 2d 808 (7th Cir. 1992); Hunt v. NationsCredit Financial Services Corp., 902 So. 2d 75 (Ala. Civ. App. 2004); Chemical Bank of Rochester v. Ashenburg, 94 Misc. 2d 64, 405 N.Y.S.2d 175 (Sup 1978).
As to the effect of a discount on the requirement that the instrument be taken for value, see § 246.

2 Overseas Credit Corp. v. Cal-Tech Systems, Inc., 20 A.D.2d 355, 247 N.Y.S.2d 252 (1st Dep't 1964), order aff'd, 14

N.Y.2d 909, 252 N.Y.S.2d 316, 200 N.E.2d 859 (1964).

[3] Hunt v. NationsCredit Financial Services Corp., 902 So. 2d 75 (Ala. Civ. App. 2004); Chemical Bank of Rochester v. Ashenburg, 94 Misc. 2d 64, 405 N.Y.S.2d 175 (Sup 1978).

[4] Hunt v. NationsCredit Financial Services Corp., 902 So. 2d 75 (Ala. Civ. App. 2004).

[5] In re Nusor, 123 B.R. 55, 13 U.C.C. Rep. Serv. 2d 773 (B.A.P. 9th Cir. 1991); First Am. Nat. Bank v. Christian Foundation Life Ins. Co., 242 Ark. 678, 420 S.W.2d 912, 4 U.C.C. Rep. Serv. 287 (1967); Sample v. Hundred Lakes Corp., 107 Fla. 568, 145 So. 193 (1933) (decided under former law); Security Central Nat. Bank v. Williams, 52 Ohio App. 2d 175, 6 Ohio Op. 3d 167, 368 N.E.2d 1264, 22 U.C.C. Rep. Serv. 1196 (10th Dist. Franklin County 1976). As to the need for inquiry, generally, see § 249.

[6] In re Nusor, 123 B.R. 55, 13 U.C.C. Rep. Serv. 2d 773 (B.A.P. 9th Cir. 1991).

End of Document

11 Am. Jur. 2d Bills and Notes § 252

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

4. Taking Instrument in Good Faith

§ 252. Close business association between payee and holder as related to good faith for purposes of holder-in-due-course rule

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 333, 340, 341

Under the "close connection" doctrine, in the context of negotiable instrument transactions, a transferee does not take an instrument in good faith when the transferee is so closely connected with the transferor that the transferee may be charged with knowledge of an infirmity in the underlying transaction.[1] A close business association between the payee and one who purchases an instrument from the payee may imply knowledge of such facts as to show bad faith or render the purchaser such a participant in the transaction between the payee and the maker as to preclude the purchaser being a holder in due course of the instrument.[2] The typical example is a finance company that customarily purchases paper signed by customers of a particular seller of goods or services, and usually furnishes the seller with forms of notes and contracts.[3] Thus, a finance company that finances a dealer, and furnishes the dealer with printed forms for retail installment contracts and promissory notes, bearing the company's name, and, following a sale by the dealer, pays the dealer and takes the customer's note, does so with notice of its infirmities, since the finance company is so closely connected with the entire transaction that it cannot be said to be an innocent purchaser of the note.[4] On the other hand, a buyer of a promissory note and deed of trust from a lender is a holder in due course, where nothing indicates that the buyer was in collusion with the lender to engage in predatory lending practices, and the other conditions for being a holder in due course are met.[5] Similarly, a corporate relationship between a trust and company that sold the trust a mortgage note did not defeat the trust's status as a holder in due course, where the trust took the note and deed of trust for value and without actual knowledge of any wrongdoing or fraud.[6]

Observation:

The holder-in-due-course doctrine has been abolished with respect to many consumer credit transactions as a matter of both state and federal law, and the holder in due course rule under the Uniform Commercial Code is subject to those laws.[7]

Footnotes

1 C & J Vantage Leasing Co. v. Outlook Farm Golf Club, LLC, 784 N.W.2d 753 (Iowa 2010).

2 Arcanum Nat. Bank v. Hessler, 69 Ohio St. 2d 549, 23 Ohio Op. 3d 468, 433 N.E.2d 204, 33 U.C.C. Rep. Serv. 604 (1982).
Where a holder has aided and counseled the payee in its business matters to such an extent that the holder is bound to know the circumstances surrounding the instrument, the holder cannot be regarded as a holder in due course and is bound by the maker's defense against the payee. Commercial Credit Corp. v. Orange County Mach. Works, 34 Cal. 2d 766, 214 P.2d 819 (1950).

3 Vasquez v. Superior Court, 4 Cal. 3d 800, 94 Cal. Rptr. 796, 484 P.2d 964, 9 U.C.C. Rep. Serv. 11, 53 A.L.R.3d 513 (1971); Morgan v. Reasor Corp., 69 Cal. 2d 881, 73 Cal. Rptr. 398, 447 P.2d 638 (1968).

4 Mutual Finance Co. v. Martin, 63 So. 2d 649, 44 A.L.R.2d 1 (Fla. 1953).

5 Stuckey v. The Provident Bank, 912 So. 2d 859, 56 U.C.C. Rep. Serv. 2d 867 (Miss. 2005).

6 Deutsche Bank Trust Company Americas v. Samora, 2013 COA 81, 321 P.3d 590 (Colo. App. 2013).

7 § 216.

End of Document

11 Am. Jur. 2d Bills and Notes § 253

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

4. Taking Instrument in Good Faith

§ 253. Application to financial institutions of good faith standard for status as holder in due course

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 337

A.L.R. Library

What constitutes taking instrument in good faith, and without notice of infirmities or defenses, to support holder-in-due-course status, under U.C.C. sec. 3-302, 36 A.L.R.4th 212

Under the objective standard of good faith,[1] the size of the check and the location of the payor bank are factors that a jury may consider when deciding whether a depositary bank is a holder in due course.[2]

A bank observed reasonable commercial standards, also required to demonstrate good faith,[3] when it gave immediate credit to a customer when the customer deposited a check, and thus was a holder in due course, where the drawer issued a stop-payment order and the customer failed to cover the stopped check, since the customer had always previously deposited funds to cover overdrafts, and the bank did not have any reason to suspect that there would be any problem if immediate credit were extended in this instance.[4] Similarly, a depository bank acted in good faith when it made funds available to an account holder on the first business day after a check was deposited, and thus the bank was a holder in due course of the check, even though it had discretion to delay making funds available for up to six business days, where there was no evidence indicating that the check's authenticity should have been called into question or that the bank took the check with any particular notice.[5] A bank's act of depositing a check of its debtor directly to his account—rather than into a special account over which the bank had control—did not constitute bad faith on the bank's part, and the bank became a holder in due course when it honored checks drawn by the depositor exceeding the amount of the deposited check, notwithstanding that some of

the checks were payable to the bank in partial liquidation of that debt.[6] On the other hand, a depository bank was not entitled to holder-in-due-course status, where it did not act according to reasonable commercial standards of fair dealing, when it failed to put a hold on the funds even though the value of the checks exceeded the bank's threshold for a discretionary hold and the checks were drawn on an out-of-state bank.[7]

Procedures that a check cashing store used with respect to a $10,000 check issued, through fraudulent inducement, by a 93-year-old maker to the indorser as part of financial investment scam did not comport with reasonable commercial standards of fair dealing, where the store did not authenticate the check with its maker before releasing funds to the indorser, who did not have a history with the store of cashing checks of similar amounts without incident, but the store's supervisor made a discretionary judgment to release the funds based on the fact that the check was in the envelope of a well-known express mail carrier.[8]

A credit card processor that obtained unauthorized checks written by a bookkeeper on the employer's account, for payment of the bookkeeper's personal credit card debt, was a holder in due course without notice, where the affidavit of the processor's representative established that it acted in good faith with honesty and observance of reasonable commercial standards of fair dealing, by establishing that it had no reason to suspect there was problem or that the bookkeeper was a fiduciary, the checks appeared to be authentic and did not have any facial irregularities, payment of the credit card debt could have been a legitimate reimbursement by the employer, and checks were drafted over a seven-year period, without any complaint from the employer.[9]

Footnotes

1 § 248.

2 Maine Family Federal Credit Union v. Sun Life Assur. Co. of Canada, 1999 ME 43, 727 A.2d 335, 37 U.C.C. Rep. Serv. 2d 875 (Me. 1999).

3 § 248.

4 Mid Wisconsin Bank v. Forsgard Trading, Inc., 2003 WI App 186, 266 Wis. 2d 685, 668 N.W.2d 830, 53 U.C.C. Rep. Serv. 2d 898 (Ct. App. 2003).

5 Wells Fargo Bank NA v. Ferruggio Insurance Services of LA Incorporated, 358 F. Supp. 3d 887, 97 U.C.C. Rep. Serv. 2d 894 (D. Ariz. 2019).

6 Exchange Nat. Bank of Winter Haven v. Beshara, 236 So. 2d 198, 7 U.C.C. Rep. Serv. 1146 (Fla. 2d DCA 1970).

7 Maine Family Federal Credit Union v. Sun Life Assur. Co. of Canada, 1999 ME 43, 727 A.2d 335, 37 U.C.C. Rep. Serv. 2d 875 (Me. 1999).

8 Any Kind Checks Cashed, Inc. v. Talcott, 830 So. 2d 160, 48 U.C.C. Rep. Serv. 2d 800 (Fla. 4th DCA 2002).

9 United Catholic Parish Schools of Beaver Dam Educational Ass'n v. Card Services Center, 2001 WI App 229, 248 Wis. 2d 463, 636 N.W.2d 206, 46 U.C.C. Rep. Serv. 2d 754 (Ct. App. 2001).

11 Am. Jur. 2d Bills and Notes § 254

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

4. Taking Instrument in Good Faith

§ 254. Good faith of holder of negotiable instrument as question for court or jury

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 337

It is generally for the jury to determine whether the holder of an instrument took it in good faith.[1]

All of the circumstances must be considered in determining whether the transferee took the paper in good faith so as to satisfy that element of being a holder in due course.[2] In determining the issue of good faith regarding the status of one as a holder in due course, the jury must decide whether the circumstances under which the purported holder acquired the instrument were such that a reasonable person could have participated in the transaction and been "honest in fact" in believing that the sale of the instrument was legitimate; this conclusion depends on an assessment of the purported holder's credibility.[3]

Where there is no evidence that the taker failed to act in good faith, it is to be concluded that the taker did act in good faith.[4] Where the evidence is undisputed and conclusive, it is the court's duty to decide this point as a matter of law, since any other rule would impair the negotiability of instruments and seriously impair commercial transactions.[5]

Footnotes

1 Manufacturers & Traders Trust Co. v. Murphy, 369 F. Supp. 11, 13 U.C.C. Rep. Serv. 1064 (W.D. Pa. 1974), aff'd, 517 F.2d 1398 (3d Cir. 1975); Sample v. Hundred Lakes Corp., 107 Fla. 568, 145 So. 193 (1933); McCarthy v. Kasperak, 3 Ohio App. 3d 206, 444 N.E.2d 472, 35 U.C.C. Rep. Serv. 540 (8th Dist. Cuyahoga County 1981).

2 McCarthy v. Kasperak, 3 Ohio App. 3d 206, 444 N.E.2d 472, 35 U.C.C. Rep. Serv. 540 (8th Dist. Cuyahoga County 1981).
Even though a bank may swear it acted in good faith, a jury may decide that it acted in bad faith after considering of

the facts and circumstances in the particular case. Choo Choo Tire Service, Inc. v. Union Planters Nat. Bank, 231 Ga. App. 346, 498 S.E.2d 799, 35 U.C.C. Rep. Serv. 2d 924 (1998).

[3] McCarthy v. Kasperak, 3 Ohio App. 3d 206, 444 N.E.2d 472, 35 U.C.C. Rep. Serv. 540 (8th Dist. Cuyahoga County 1981).

[4] Ashland State Bank v. Elkhorn Racquetball, Inc., 246 Neb. 411, 520 N.W.2d 189, 24 U.C.C. Rep. Serv. 2d 968 (1994).

[5] Manufacturers & Traders Trust Co. v. Murphy, 369 F. Supp. 11, 13 U.C.C. Rep. Serv. 1064 (W.D. Pa. 1974), aff'd, 517 F.2d 1398 (3d Cir. 1975).

End of Document

11 Am. Jur. 2d Bills and Notes § 255

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

5. Taking Instrument Without Notice of Claims and Defenses

a. In General

§ 255. Taking instrument without notice of claims and defenses, generally

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 332

A.L.R. Library

What constitutes taking instrument in good faith, and without notice of infirmities or defenses, to support holder-in-due-course status, under U.C.C. sec. 3-302, 36 A.L.R.4th 212

Forms

Forms relating to draft taken without notice of defect or defense, see Am. Jur. Pleading and Practice Forms, Commercial Code [Westlaw®(r) Search Query]

To be a holder in due course, a holder must take the instrument without notice that the instrument is overdue or has been dishonored,[1] that the instrument contains an unauthorized signature or has been altered,[2] or of any claim to the instrument[3] or of any defense or claim in recoupment.[4]

A transferee who takes a note with notice of a defense on the part of any person is not a holder in due course.[5]

As generally defined in the Uniform Commercial Code, and subject to the provision on notice to an organization,[6] a person has "notice" of a fact if the person:[7]

(1) has actual knowledge of it;

(2) has received a notice or notification of it; or

(3) from all the facts and circumstances known to the person at the time in question, has reason to know that it exists.
In turn, "knowledge" means actual knowledge, and "knows" has a corresponding meaning.[8] "Discover," "learn," or words of similar import refer to knowledge rather than to reason to know.[9]

A person "receives" a notice or notification when it comes to that person's attention; or it is delivered in a form reasonable under the circumstances at the place of business through which the contract was made, or at another location held out by that person as the place for receipt of communications of that type.[10]

The forgoing definition applies to the question whether a holder had notice when the check at issue was negotiated.[11] The same standard of "subjective, actual knowledge" of the claim or defense applies to both the requirements that holder must the take the instrument in good faith and without notice of any defense to enforcement.[12] The definition of notice includes reason to know,[13] and it has been said that a purchaser of a note has constructive notice that the note is overdue, and thus cannot be a holder in due course, if it has reason to know that any part of the principal amount is overdue.[14] However, neither constructive knowledge of a defense or claim, in the sense of what a reasonable person in the holder's position should have known or should have inquired about,[15] nor mere suspicion of a defect or defense is sufficient, as there must be actual knowledge of a defense or of facts giving rise to a defense such that the taking of the instrument would amount to bad faith.[16]

Notice, knowledge, or a notice or notification received by an organization is effective for a particular transaction from the time it is brought to the attention of the individual conducting that transaction and, in any event, from the time it would have been brought to the individual's attention if the organization had exercised due diligence. An organization exercises due diligence if it maintains reasonable routines for communicating significant information to the person conducting the transaction and there is reasonable compliance with those routines. Due diligence does not require that an individual acting for the organization communicate information unless the communication is part of the individual's regular duties or the individual has reason to know of the transaction and that the transaction would be materially affected by the information.[17]

Footnotes

1 §§ 260 to 263.

2 § 264.

3 §§ 265, 266.

4 U.C.C. § 3-302(a)(2)(vi)[Rev], further discussed in §§ 267 to 270.

5 Arcanum Nat. Bank v. Hessler, 69 Ohio St. 2d 549, 23 Ohio Op. 3d 468, 433 N.E.2d 204, 33 U.C.C. Rep. Serv. 604 (1982).
Notice of defenses or infirmities in a note defeats holder-in-due-course status. F.D.I.C. v. World University Inc., 978 F.2d 10, 23 Fed. R. Serv. 3d 1373 (1st Cir. 1992).

6 U.C.C. § 1-202(f)[Rev].

7 U.C.C. § 1-202(a)[Rev].

8 U.C.C. § 1-202(b)[Rev].

9 U.C.C. § 1-202(c)[Rev].

[10] U.C.C. § 1-202(e)[Rev].

[11] United Catholic Parish Schools of Beaver Dam Educational Ass'n v. Card Services Center, 2001 WI App 229, 248 Wis. 2d 463, 636 N.W.2d 206, 46 U.C.C. Rep. Serv. 2d 754 (Ct. App. 2001).

[12] In re AppOnline.com, Inc., 321 B.R. 614 (E.D. N.Y. 2003), judgment aff'd, 128 Fed. Appx. 171 (2d Cir. 2004); Bankers Trust (Delaware) v. 236 Beltway Inv., 865 F. Supp. 1186, 26 U.C.C. Rep. Serv. 2d 776 (E.D. Va. 1994).
The duty of inquiry under the good faith standard is discussed in § 249.

[13] U.C.C. § 1-202(a)(3)[Rev].

[14] In re Trevino, 535 B.R. 110 (Bankr. S.D. Tex. 2015).
A finance company, which purchased from a broker in the business of selling commercial paper to finance companies at a profit a note in the face amount of $16,260 for $11,000 had "reason to know" that there was a good defense—usury—against the note. Winter & Hirsch, Inc. v. Passarelli, 122 Ill. App. 2d 372, 259 N.E.2d 312, 7 U.C.C. Rep. Serv. 1210 (1st Dist. 1970).

[15] In re AppOnline.Com, Inc., 290 B.R. 1, 49 U.C.C. Rep. Serv. 2d 1241 (Bankr. E.D. N.Y. 2003).

[16] Cardarelli v. Scodek Construction Corp., 304 A.D.2d 894, 758 N.Y.S.2d 188 (3d Dep't 2003).
Grounds for suspicion about a check will not always prevent one from taking the check as a holder in due course. New Randolph Halsted Currency Exchange, Inc. v. Regent Title Ins. Agency, LLC, 405 Ill. App. 3d 923, 345 Ill. Dec. 844, 939 N.E.2d 1024, 73 U.C.C. Rep. Serv. 2d 341 (1st Dist. 2010).
The mere fact that warehouse lenders that purchased notes from the debtor may have harbored suspicions about certain of the debtor's practices, or that a prudent warehouse lender allegedly would have undertaken more due diligence, did not affect their good faith, or preclude them from qualifying as holders in due course of those notes, where the lenders did not have any knowledge that the debtor would fail to pay the closing agent. In re AppOnline.com, Inc., 285 B.R. 805, 49 U.C.C. Rep. Serv. 2d 531 (Bankr. E.D. N.Y. 2002), order aff'd, 321 B.R. 614 (E.D. N.Y. 2003), judgment aff'd, 128 Fed. Appx. 171 (2d Cir. 2004).

[17] U.C.C. § 1-202(f)[Rev].
In a case in which an employer discovered that an employee was embezzling funds, but by the time it notified a stockbroker (with whom the employee had maintained a personal account) of the embezzlement, the funds in the account were withdrawn, the question was not just whether the notice to the broker was sufficient to charge the brokerage firm, so as to preclude it from being a holder in due course of checks presented by the embezzler, but also whether the firm was charged with information in its files that the individual broker never saw; information in those files would be imputed to the broker, for the purpose of the definition described above, only if the firm was negligent in not bringing it to the broker's attention, since he was "the individual conducting that transaction." Jelmoli Holding, Inc. v. Raymond James Financial Services, Inc., 470 F.3d 14, 61 U.C.C. Rep. Serv. 2d 291 (1st Cir. 2006).

End of Document

11 Am. Jur. 2d Bills and Notes § 256

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

5. Taking Instrument Without Notice of Claims and Defenses

a. In General

§ 256. Imputation of knowledge of claims or defenses to principal, for purposes of holder-in-due-course rule

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 340

The general rule that notice to an agent is ordinarily notice to the principal[1] has been applied in the context of negotiable instruments.[2] For instance, where a company in the business of buying secured promissory notes was the agent of lending company, the agent's knowledge of the mortgagee's cancellation of the sale of the promissory note and demand for its return was imputed to the lending company and precluded it from qualifying for holder-in-due-course status.[3] However, notice will not be imputed to a principal where the evidence shows that the agent is acting adversely to the principal, or is acting for himself or herself.[4] Of course, knowledge will not be imputed where an agency relationship does not exist between the seller and purchaser of a note.[5]

Footnotes

1 Am. Jur. 2d, Agency § 255.

2 As to notice received by an organization, see § 255.

3 First Nat. Acceptance Co. v. Bishop, 187 S.W.3d 710 (Tex. App. Corpus Christi 2006).

4 Corporacion Peruana de Aeropuertos y Aviacion Comercial v. Boy, 180 So. 2d 503 (Fla. 2d DCA 1965); Matteawan Mfg. Co. v. Chemical Bank & Trust Co., 244 A.D. 404, 279 N.Y.S. 495 (1st Dep't 1935), aff'd as modified on other grounds, 272 N.Y. 411, 3 N.E.2d 845 (1936).

[5] Midfirst Bank, SSB v. C.W. Haynes & Co., Inc., 893 F. Supp. 1304, 27 U.C.C. Rep. Serv. 2d 1292 (D.S.C. 1994), judgment aff'd, 87 F.3d 1308 (4th Cir. 1996); Gonzales v. American Title Co. of Houston, 104 S.W.3d 588 (Tex. App. Houston 1st Dist. 2003).

End of Document

11 Am. Jur. 2d Bills and Notes § 257

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

5. Taking Instrument Without Notice of Claims and Defenses

a. In General

§ 257. Record notice of claim or defense, for purposes of holder-in-due-course rule

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 332, 336.1

The public filing or recording of a document does not of itself constitute notice of a defense, claim in recoupment, or claim to the instrument.[1] Thus, "notice," in the context of what bars a taker from being a holder in due course, requires actual knowledge of the facts that give notice.[2] The provision on record notice manifests a reluctance to tie negotiable instruments to the doctrine of constructive notice.[3] In other words, the constructive notice arising from a recording is not the notice required by the Uniform Commercial Code to preclude holder-in-due-course status.[4] For example, the fact that a bank subscribes to a service that reports the filing of financing statements does not establish that the bank had notice that a check that it cashed represented the proceeds from the sale of collateral covered by a security interest, where so many months intervened that the "notice" may have been forgotten.[5]

Footnotes

1 U.C.C. § 3-302(b)[Rev].
One taking a negotiable instrument is not precluded from taking it as a holder in due course by the operation of a record notice. Taylor v. American Nat. Bank of Pensacola, 64 Fla. 525, 60 So. 783 (1913).

2 Indyk v. Habib Bank Ltd., 694 F.2d 54, 35 U.C.C. Rep. Serv. 158 (2d Cir. 1982).

3 Saloga v. Central Kansas Credit Union, 245 Kan. 668, 783 P.2d 339, 10 U.C.C. Rep. Serv. 2d 866 (1989).

4 National Sec. Fire & Cas. Co. v. Mazzara, 289 Ala. 542, 268 So. 2d 814, 11 U.C.C. Rep. Serv. 1006 (1972).

[5] McCook County Nat. Bank v. Compton, 558 F.2d 871, 21 U.C.C. Rep. Serv. 1360 (8th Cir. 1977).
The doctrine of forgotten notice is discussed in § 259.

End of Document

11 Am. Jur. 2d Bills and Notes § 258

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

5. Taking Instrument Without Notice of Claims and Defenses

a. In General

§ 258. Time of notice of claim or defense, for purposes of holder-in-due-course rule

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 334

Forms

Forms relating to a reasonable opportunity to act, see Am. Jur. Pleading and Practice Forms, Commercial Code [Westlaw®(r) Search Query]

The proper time for determining whether a recipient of a negotiable instrument has notice of a claim or defense so as to preclude the recipient's status as a holder in due course is the time of negotiation of the instrument to the holder.[1] To be effective, notice to a purchaser must be received at such time and in such manner as to give a reasonable opportunity to act on it.[2] The reasonable opportunity to act on that knowledge must be when the instrument was negotiated,[3] and the holder received possession of it.[4] Knowledge or notice that is acquired after the taker has become the holder of the instrument is immaterial; otherwise stated, subsequently acquired knowledge does not operate retroactively so as to disentitle the holder from the status as a holder in due course.[5] So, it is immaterial to one's status that the transferee of a note learned of the transferor's fraud after the instrument had been negotiated to the transferee under circumstances making the transferee a holder in due course.[6]

Whether a holder of notes in a series has such knowledge as bars the holder from being a holder in due course must be determined with respect to each note as of the time that it was taken; the knowledge that had been acquired by the time the last note was taken may not be imputed to the taking of the earlier notes; therefore, the later-acquired knowledge does not bar holder-in-due-course status with respect to a note that had been taken before such knowledge was acquired.[7]

When a later note transaction is such that the original note is discharged, the creditor's status with respect to the original note is not retained by the subsequent note, and the creditor must establish that he or she is a favored holder of the latter note when a defense is raised.[8]

Footnotes

1 Allison-Kesley Ag Center, Inc. v. Hildebrand, 485 N.W.2d 841, 19 U.C.C. Rep. Serv. 2d 480 (Iowa 1992); RR Maloan Investments, Inc. v. New HGE, Inc., 428 S.W.3d 355, 83 U.C.C. Rep. Serv. 2d 311 (Tex. App. Houston 14th Dist. 2014) (in which an employee of a company took a check from the payee in exchange for cash in the normal course of business).

2 U.C.C. § 3-302(f)[Rev].

3 United Catholic Parish Schools of Beaver Dam Educational Ass'n v. Card Services Center, 2001 WI App 229, 248 Wis. 2d 463, 636 N.W.2d 206, 46 U.C.C. Rep. Serv. 2d 754 (Ct. App. 2001) (check).

4 Wells Fargo Bank NA v. Ferruggio Insurance Services of LA Incorporated, 358 F. Supp. 3d 887, 97 U.C.C. Rep. Serv. 2d 894 (D. Ariz. 2019) (the critical time for determining whether a holder had notice of defenses to the payment of an instrument is when the party came into possession of the instrument as a holder); Provident Bank v. MorEquity, Inc., 262 Ga. App. 331, 585 S.E.2d 625, 50 U.C.C. Rep. Serv. 2d 1205 (2003) (the purchaser of a promissory note secured by a mortgage was not a holder in due course, where when the purchaser eventually received possession of the note from the warehouse lender, it received at the same time a bailment letter in which the warehouse lender provided notice of its security interest).

5 Mann v. Andrus, 169 Cal. App. 2d 455, 337 P.2d 473 (2d Dist. 1959); Kroh v. Pronto Petroleum Co., 536 P.2d 860, 17 U.C.C. Rep. Serv. 804 (Colo. App. 1975); Tipton v. Heeren, 109 Nev. 920, 859 P.2d 465 (1993).

6 Universal C.I.T. Credit Corp. v. Ingel, 347 Mass. 119, 196 N.E.2d 847, 3 U.C.C. Rep. Serv. 303 (1964).

7 Slaughter v. Jefferson Federal Sav. and Loan Ass'n, 538 F.2d 397, 19 U.C.C. Rep. Serv. 171 (D.C. Cir. 1976), also published at, 19 U.C.C. Rep. Serv. 534 (D.C. Cir. 1976).

8 Lazere Financial Corp. v. Crystal Mart, Inc., 78 Misc. 2d 379, 357 N.Y.S.2d 973, 14 U.C.C. Rep. Serv. 1173 (N.Y. City Civ. Ct. 1974).

End of Document

11 Am. Jur. 2d Bills and Notes § 259

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

5. Taking Instrument Without Notice of Claims and Defenses

a. In General

§ 259. Forgotten notice of claim or defense, for purposes of holder-in-due-course rule

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 334

A.L.R. Library

Notice which has been forgotten as affecting status as holder in due course, 89 A.L.R.2d 1330

Where one taking an instrument contends that he or she did not have notice of the claim or defense at the time of negotiation, although he or she had notice at a prior time, the doctrine of "forgotten notice" may be applicable; if it is found by the trier of fact that the earlier notice had in fact and in good faith been forgotten by the later time when the paper was taken, the forgotten notice is not effective.[1] In other words, it may be a jury question whether the taker had forgotten the notice or inadvertently failed to inquire, and whether that would constitute mere negligence and not bad faith, which would destroy the taker's status as a holder in due course.[2] However, application of the doctrine has been denied where its strict application would be unrealistic, and it is applied with great caution in the case of a simple note, as contrasted with a bond of general issue.[3]

Footnotes

[1] McCook County Nat. Bank v. Compton, 558 F.2d 871, 21 U.C.C. Rep. Serv. 1360 (8th Cir. 1977).

[2] Graham v. White-Phillips Co., 296 U.S. 27, 56 S. Ct. 21, 80 L. Ed. 20, 102 A.L.R. 24 (1935).
As to the effect of negligence on the existence of good faith, see § 250.

[3] First Nat. Bank of Odessa v. Fazzari, 10 N.Y.2d 394, 223 N.Y.S.2d 483, 179 N.E.2d 493, 89 A.L.R.2d 1324 (1961).

End of Document

11 Am. Jur. 2d Bills and Notes § 260

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

5. Taking Instrument Without Notice of Claims and Defenses

b. Notice that Instrument is Overdue or Has Been Dishonored

§ 260. Notice that instrument is overdue or has been dishonored, generally

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 344, 347.1 to 350

Forms

Forms relating to lack of notice, generally, see Am. Jur. Pleading and Practice Forms, Commercial Code [Westlaw®(r) Search Query]

A holder in due course must have taken an instrument without notice that it is overdue or has been dishonored or that there is an uncured default with respect to the payment of another instrument issued as part of the same series.[1] Thus, one may not be a holder in due course of a note taken after maturity[2] or with regard to the overdue installment payments.[3] A purchaser of a note has constructive notice that the note is overdue, and thus cannot be a holder in due course, if it has reason to know that any part of the principal amount is overdue.[4] However, the fact that a transferee took an instrument after an installment was overdue does not show that the transferee did not act in good faith, when there is nothing to show that the transferee knew that it was overdue or of any defense at the time of the transfer.[5] Also, the fact that the holder took several notes at a time when the first was overdue does not prevent the holder from being a holder in due course as to those notes that were not overdue.[6]

The transferee of a note is not required to establish affirmatively that the instrument was not in default at the time that it was transferred to him or her.[7]

Observation:

Under the "shelter" doctrine incorporated in Article 3, a holder who acquires an instrument from a holder in due course or from a successor in interest of a holder in due course, even with notice that it is overdue or has been dishonored, may assert the rights of a holder in due course.[8] The issue in a case where the plaintiff buys dishonored checks from a check cashing company is not whether the plaintiff, but the check casher, is a holder in due course,[9] and the efficacy of the assignment to the plaintiff is essential to asserting holder-in-due-course status after the instrument has been dishonored.[10]

Footnotes

1 U.C.C. § 3-302(a)(2)(iii)[Rev].
A foreclosure trustee was a holder in due course of a note, as it had taken the debtor's note without knowledge of his incapacity or fraud defenses, and before the note was overdue or in default. Erkins v. Alaska Trustee, LLC, 355 P.3d 516 (Alaska 2015).
The assignee of a promissory note was not a "holder in due course" where the assignee did not pay value for the note and had notice that the note was overdue. Walker v. Probandt, 25 Neb. App. 30, 902 N.W.2d 468, 93 U.C.C. Rep. Serv. 2d 838 (2017), review denied, (May 8, 2018) and cert. denied, 139 S. Ct. 333, 202 L. Ed. 2d 223 (2018).
A purchaser of a note who knew at the time of purchase that the note was overdue does not qualify as a holder in due course, but may still recover on the indebtedness, subject to any claims or defenses available to the obligor, including those defenses that are available at common law against enforcement of a contract. World Help v. Leisure Lifestyles, Inc., 977 S.W.2d 662 (Tex. App. Fort Worth 1998).
A buyer of a check could not himself be a holder in due course, where the buyer took the check by assignment after it was dishonored, and there was a "stop payment" order stamped on the check's face. Triffin v. Quality Urban Housing Partners, 352 N.J. Super. 538, 800 A.2d 905, 48 U.C.C. Rep. Serv. 2d 651 (App. Div. 2002).
As to what constitutes notice, see § 255.

2 § 263.

3 Coleman Music and Games Co., Inc. v. McDaniel, 411 So. 2d 193 (Fla. 5th DCA 1981).
As to when an installment note is overdue after a default, see § 262.

4 In re Trevino, 535 B.R. 110 (Bankr. S.D. Tex. 2015) (under Texas law).

5 DH Cattle Holdings Co. v. Smith, 195 A.D.2d 202, 607 N.Y.S.2d 227, 22 U.C.C. Rep. Serv. 2d 799 (1st Dep't 1994).
An investor, assigned a mortgage by an investment corporation in payment of a claim against an affiliate company, was a holder in due course of a promissory note that was executed with the mortgage, where the note was taken without notice that it was overdue or dishonored and without notice of any claim to or defense against it by any person. Thomas v. State Mortg., Inc., 176 Mich. App. 157, 439 N.W.2d 299, 9 U.C.C. Rep. Serv. 2d 1276 (1989).

6 Farmers and Merchants State Bank v. Mann, 87 S.D. 90, 203 N.W.2d 173 (1973).

7 First Nat. Bank of Tribune, Kan. v. Lohman, 827 P.2d 583, 16 U.C.C. Rep. Serv. 2d 1098 (Colo. App. 1992).

8 §§ 224 to 226.

9 Triffin v. Quality Urban Housing Partners, 352 N.J. Super. 538, 800 A.2d 905, 48 U.C.C. Rep. Serv. 2d 651 (App. Div. 2002).

10 Triffin v. Automatic Data Processing, Inc., 394 N.J. Super. 237, 926 A.2d 362 (App. Div. 2007).
As to the nature of the assignment required under the shelter rule, see § 226.

End of Document

11 Am. Jur. 2d Bills and Notes § 261

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

5. Taking Instrument Without Notice of Claims and Defenses

b. Notice that Instrument is Overdue or Has Been Dishonored

§ 261. When is demand instrument overdue

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 347.1, 348

A.L.R. Library

What constitutes, under the Uniform Negotiable Instruments Law or Commercial Code, a reasonable time for taking a demand instrument, so as to support the taker's status as holder in due course, 10 A.L.R.3d 1199

An instrument payable on demand becomes overdue at the earliest of the following times:[1]

(1) on the day after the day demand for payment is duly made;

(2) if the instrument is a check, 90 days after its date;

(3) if the instrument is not a check, when the instrument has been outstanding for a period after its date that is unreasonably long under the circumstances of the particular case, in light of the nature of the instrument and usage of the trade.

Comment:

The described provision requires that the trier of fact look at both the circumstances of the particular case, and the nature of the instrument and trade usage. Whether a demand note is stale may vary a great deal, depending on the facts of the particular case.[2]

A check becomes overdue 90 days after the date it was actually issued, not 90 days after the date on it; thus, a check misdated with the prior year is not necessarily overdue.[3]

Footnotes

1 U.C.C. § 3-304(a)[Rev].

2 U.C.C. § 3-304[Rev] Official Comment 1.

3 Commerce Bank, N.A. v. Rickett, 329 N.J. Super. 379, 748 A.2d 111, 41 U.C.C. Rep. Serv. 2d 231 (App. Div. 2000).

End of Document

11 Am. Jur. 2d Bills and Notes § 262

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

5. Taking Instrument Without Notice of Claims and Defenses

b. Notice that Instrument is Overdue or Has Been Dishonored

§ 262. When is instrument payable at definite time overdue

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 347.1, 348

Forms

Forms relating to holder and installment note, generally, see Am. Jur. Pleading and Practice Forms, Commercial Code [Westlaw®(r) Search Query]

With respect to an instrument payable at a definite time, the instrument is overdue in accordance with the following rules:[1]

(1) if the principal is payable in installments and a due date has not been accelerated, the instrument becomes overdue upon default under the instrument for nonpayment of an installment, and the instrument remains overdue until the default is cured;

(2) if the principal is not payable in installments and the due date has not been accelerated, the instrument becomes overdue on the day after the due date;

(3) if a due date with respect to principal has been accelerated, the instrument becomes overdue on the day after the accelerated due date.

Unless the due date of principal has been accelerated, an instrument does not become overdue if there is default in payment of interest but no default in payment of principal.[2]

Observation:

The rationale is that interest payments are often in default even though there is no infirmity in the transaction.[3]

Footnotes

1 U.C.C. § 3-304(b)[Rev].

2 U.C.C. § 3-304(c)[Rev].
A holder purchased a note without notice that it was overdue and subject to an uncured default, as required for holder-in-due-course status, even though the maker of the note had not made any of the required interest payments, since the note's principal had not yet become due at the time of the sale. Cadle Co. v. Ginsburg, 51 Conn. App. 392, 721 A.2d 1246, 37 U.C.C. Rep. Serv. 2d 684 (1998).

3 Frisch, Lawrence's Anderson on the Uniform Commercial Code § 3-304:10 (3d ed.).

End of Document

11 Am. Jur. 2d Bills and Notes § 263

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

5. Taking Instrument Without Notice of Claims and Defenses

b. Notice that Instrument is Overdue or Has Been Dishonored

§ 263. Holder of note purchased after maturity as holder in due course

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 348

A holder is not a holder in due course when the note is purchased after maturity[1] and while in default,[2] unless the shelter rule applies.[3] The rationale for the rule that a taker after maturity is not a holder in due course is that the age of the paper is a circumstance that should put the taker on inquiry that there must be some matter of defense, even though the mere maturity of the paper does not in itself give any indication of any specific defense.[4]

Footnotes

1 St. Bernard Sav. and Loan Ass'n v. Cella, 826 F. Supp. 985 (E.D. La. 1993); Cadle Co. v. DeVincent, 57 Mass. App. Ct. 13, 781 N.E.2d 817, 49 U.C.C. Rep. Serv. 2d 1261 (2003).

2 L & S Enterprises, Inc. v. Miami Tile & Terrazzo, Inc., 148 So. 2d 299 (Fla. 3d DCA 1963).

3 §§ 224 to 226.

4 Copeland v. Anderson, 15 Ariz. App. 60, 485 P.2d 1177 (Div. 1 1971).

End of Document

11 Am. Jur. 2d Bills and Notes § 264

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

5. Taking Instrument Without Notice of Claims and Defenses

c. Notice of Unauthorized Signature or Alteration

§ 264. Notice of unauthorized signature or alteration as affecting status as holder in due course, generally

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 332

Forms

Forms relating to notice of unauthorized signature, material alteration, or signature obtained by fraud, see Am. Jur. Pleading and Practice Forms, Commercial Code [Westlaw®(r) Search Query]

A holder in due course must have taken an instrument without notice that the instrument contains an unauthorized signature or has been altered.[1]

Comment:

The requirement that a holder take an instrument without notice of forgery or alteration is stated separately from the requirement that a holder take without notice of defenses to the instrument because forgery and alteration are not technically defenses under that section of the revised Article 3 enumerating defenses and claims in recoupment.[2]

A bank that was the payee on checks presented by the drawer's agent in an embezzlement scheme is under a common-law duty to inquire into the agent's authority, and is not a holder in due course for purposes of defending against liability to the drawer.[3] On the other hand, a bank at which a limited partnership had an account was a holder in due course of checks that were drawn on the partnership's account by the partnership's bookkeeper, who was an authorized signatory on the account, where a certificate of resolution filed with the bank instructed it to honor all checks drawn on the partnership's account that bore the bookkeeper's signature.[4] The fact that checks were drawn in a corporation's name by the corporation's chief executive officer was insufficient to show that the payee had actual knowledge that the chief executive officer lacked the authority to use corporate funds for the purposes at issue and that the funds had been secretly diverted from the corporation's regular account to preclude the payee from asserting holder-in-due-course status.[5]

Footnotes

1 U.C.C. § 3-302(a)(2)(iv)[Rev].
As to instruments bearing apparent evidence of forgery or alteration, see §§ 235 to 238.
As to what constitutes notice, see § 255.

2 U.C.C. § 3-302[Rev] Official Comment 2, referring to U.C.C. § 3-305(a)[Rev].

3 Dalton & Marberry, P.C. v. NationsBank, N.A., 982 S.W.2d 231, 37 U.C.C. Rep. Serv. 2d 1 (Mo. 1998).
As to whether a payee bank can be a holder in due course of a check presented by someone other than the drawer, generally, see § 221.

4 Dalton Point, L.P. v. Regions Bank, Inc., 287 Ga. App. 468, 651 S.E.2d 549, 63 U.C.C. Rep. Serv. 2d 836 (2007).

5 Transglobal Marketing Corp. v. Derfner & Mahler, LLP, 246 A.D.2d 482, 667 N.Y.S.2d 751 (1st Dep't 1998).

11 Am. Jur. 2d Bills and Notes § 265

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

5. Taking Instrument Without Notice of Claims and Defenses

d. Notice of Claim to Instrument

§ 265. Notice of claim to instrument as affecting status as holder in due course, generally

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 332

To qualify as a holder in due course, a holder must have taken an instrument without notice of any claim to the instrument described in the provisions of Article 3 relating to claims of a property or possessory right in an instrument or its proceeds, including a claim to rescind negotiation and to recover the instrument or its proceeds.[1] This includes such matters as taking with notice of the maker's absolute right to rescind[2] or of the fact that the check was conditionally delivered subject to its acceptance as settlement of an account.[3] It also includes taking a cashier's check after a payee was notified by the bank that issued it that it had been purchased with stolen funds.[4]

Reminder:

Public filing or recording of a document does not, of itself, constitute notice of a claim to the instrument.[5]

Footnotes

1 U.C.C. § 3-302(a)(2)(v)[Rev] referring to U.C.C. § 3-306[Rev].

A law firm that took third-party accounts-receivable checks that were delivered to it by a borrower, one of its clients, did not take the checks in good faith and without notice of the lender's claim to the check funds, and thus the law firm was not a holder in due course of the checks, as the lender's security interest had attached before the law firm deposited the checks in an Interest on Lawyer Trust Accounts account, and the law firm was aware of the security interest at the time of the deposits. Heartland Bank and Trust v. The Leiter Group, 2014 IL App (3d) 130498, 385 Ill. Dec. 297, 18 N.E.3d 558 (App. Ct. 3d Dist. 2014).

Purchasers of an interest in a promissory note were not holders in due course, where an investigation made by one of the purchasers into various parties' interests in the note had provided actual notice of claims against the instrument. Brantley v. Karas, 220 Va. 489, 260 S.E.2d 189, 27 U.C.C. Rep. Serv. 1332 (1979).

Since a lender did not know that checks issued by cotton buyers, which were made payable jointly to the lender and borrower, a farming business, could be subject to a possible claim by the landowner that had hired the owner of the farming business to farm cotton, the lender did not have notice of the landowner's claim, so as to preclude holder-in-due-course status. Fedeli v. UAP/Ga. Ag. Chem., Inc., 237 Ga. App. 337, 514 S.E.2d 684, 38 U.C.C. Rep. Serv. 2d 845 (1999).

[2] Merchants Mortg. & Trust Corp. v. Dawe, 754 P.2d 418 (Colo. App. 1987); First Intern. Bank of Israel, Ltd. v. L. Blankstein & Son, Inc., 59 N.Y.2d 436, 465 N.Y.S.2d 888, 452 N.E.2d 1216, 36 U.C.C. Rep. Serv. 565 (1983).

[3] Losson v. Whitson, 535 S.W.2d 406, 19 U.C.C. Rep. Serv. 1169 (Tex. Civ. App. Amarillo 1976).

[4] American Federal Sav. and Loan Ass'n v. Madison Valley Properties Inc., 1998 MT 93, 288 Mont. 365, 958 P.2d 57, 36 U.C.C. Rep. Serv. 2d 807, 77 A.L.R.5th 729 (1998).

[5] § 257.

End of Document

11 Am. Jur. 2d Bills and Notes § 266

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

5. Taking Instrument Without Notice of Claims and Defenses

d. Notice of Claim to Instrument

§ 266. Notice of claim arising out of breach of fiduciary duty as affecting status as holder in due course

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 340

If an instrument is taken from a fiduciary for payment or collection or for value, the taker has knowledge of the fiduciary status of the fiduciary, and if the represented person makes a claim to the instrument or its proceeds on the basis that the transaction of the fiduciary is a breach of fiduciary duty:

(1) notice of breach of fiduciary duty by the fiduciary is notice of the claim of the represented person[1]

(2) in the case of an instrument payable to the represented person or the fiduciary as a fiduciary, the taker has notice of the breach of fiduciary duty if the instrument is taken in payment of or as security for a debt known by the taker to be a personal debt of the fiduciary; taken in a transaction known by the taker to be for the fiduciary's personal benefit; or deposited to an account other than a fiduciary account or an account of the represented person[2]

(3) if an instrument is issued by the represented person or the fiduciary in that capacity, and made payable to the fiduciary personally, the taker does not have notice of the breach of fiduciary duty unless the taker knows of that breach[3]

(4) if an instrument is issued by the represented person or the fiduciary in that capacity, to the taker as payee, the taker has notice of the breach of fiduciary duty if the instrument is taken in payment of or as security for a debt known by the taker to be the fiduciary's personal debt; taken in a transaction known by the taker to be for the personal benefit of the fiduciary; or deposited to an account other than a fiduciary account or an account of the represented person[4]

Definition:

A "fiduciary" is an agent, trustee, partner, corporate officer or director, or other representative owing a fiduciary duty with respect to an instrument.[5] A "represented person" is the principal, beneficiary, partnership, corporation, or other person to whom the duty of a fiduciary is owed.[6]

The taker of an instrument payable to person represented by a fiduciary must have actual knowledge of the fiduciary's status as such to have notice of a breach of fiduciary duty if the instrument is deposited to an account other than the account of the fiduciary, as such, or the account of the represented person; mere "warning clues" that the individual might be a fiduciary are not sufficient.[7]

Allegations that checks were drawn to the order of a bank as payee, but were negotiated by an employee of the drawer for her own benefit, if true, generally establish adequate notice so as to preclude the bank from holder-in-due-course status on the basis of a violation of a fiduciary duty.[8] Similarly, a depository bank is not a holder in due course of checks payable to its customer that the customer's fiduciary deposited into the fiduciary's personal accounts, for purposes of the customer's conversion claim against the bank based on checks deposited into the fiduciary's personal accounts.[9]

A vendor had notice of a corporate president's breach of fiduciary duty to the corporation, precluding the vendor being a holder in due course, where the president signed a corporate note and pledged corporate property as security, but the vendor did not see or request any documentation to establish that the president had the authority to do so.[10]

Caution:

The section of the Uniform Commercial Code described above, while it describes a type of claim to an instrument,[11] provides the exclusive manner of showing notice when a breach of fiduciary duty claim is made, and the provision on competing claims[12] does not apply.[13] Therefore, a reason to know of a competing claim does not defeat holder-in-due-course status, if the holder does not have actual knowledge of the drawer's fiduciary status.[14] Also, the argument that anyone who signs a check for an entity is a fiduciary is insufficient to establish the taker's actual knowledge of that relationship.[15]

Footnotes

1 U.C.C. § 3-307(b)(1)[Rev].

2 U.C.C. § 3-307(b)(2)[Rev].
This provision of the U.C.C. will ordinarily prevail over a provision of the Uniform Fiduciaries Act, which states that a bank is not liable for allowing a known fiduciary to deposit a check into his personal account, unless the bank has "actual knowledge" of a breach of fiduciary duty. County of Macon v. Edgcomb, 274 Ill. App. 3d 432, 211 Ill. Dec. 136, 654 N.E.2d 598, 27 U.C.C. Rep. Serv. 2d 1328 (4th Dist. 1995).
Three checks embezzled from a trust by a trustee were "taken" by a bank under the Illinois Uniform Commercial Code (UCC), for the purpose of determining whether the trust's claims against the bank for negligence and breach of contract in connection with the embezzlement were displaced by the U.C.C. provision setting forth circumstances under which a person taking an instrument from a fiduciary was not deemed to be a holder in due course, where the trustee deposited the embezzled checks into his personal account at the bank. Crawford Supply Group, Inc. v. Bank of America, N.A., 829 F. Supp. 2d 636, 76 U.C.C. Rep. Serv. 2d 1 (N.D. Ill. 2011).

3 U.C.C. § 3-307(b)(3)[Rev].

4 U.C.C. § 3-307(b)(4)[Rev].

5 U.C.C. § 3-307(a)(1)[Rev].

[6] U.C.C. § 3-307(a)(2)[Rev].

[7] Fine v. Sovereign Bank, 671 F. Supp. 2d 219 (D. Mass. 2009).
As to what constitutes "knowledge," see § 255.

[8] Sun 'n Sand, Inc. v. United California Bank, 21 Cal. 3d 671, 148 Cal. Rptr. 329, 582 P.2d 920, 21 U.C.C. Rep. Serv. 2d 1003 (1978).
As to the effect of a payee bank cashing such a check, generally, see § 221.

[9] C-Wood Lumber Co., Inc. v. Wayne County Bank, 233 S.W.3d 263, 61 U.C.C. Rep. Serv. 2d 877 (Tenn. Ct. App. 2007) (decided after the effective date of amendments conforming the state's version of the U.C.C. to Revised Article 3, and noting that the employees of the bank who accepted the deposits from the customer's fiduciary knew she was a corporate officer of the customer when she made the deposits, and bank employees receiving the deposits were sufficiently concerned about the propriety of the deposits that they called the transactions to the attention of the bank's officers and requested instructions regarding how to proceed).

[10] Max Duncan Family Investments, Ltd. v. NTFN Inc., 267 S.W.3d 447 (Tex. App. Dallas 2008).

[11] United Catholic Parish Schools of Beaver Dam Educational Ass'n v. Card Services Center, 2001 WI App 229, 248 Wis. 2d 463, 636 N.W.2d 206, 46 U.C.C. Rep. Serv. 2d 754 (Ct. App. 2001).

[12] § 265.

[13] Jelmoli Holding, Inc. v. Raymond James Financial Services, Inc., 470 F.3d 14, 61 U.C.C. Rep. Serv. 2d 291 (1st Cir. 2006).

[14] Jelmoli Holding, Inc. v. Raymond James Financial Services, Inc., 470 F.3d 14, 61 U.C.C. Rep. Serv. 2d 291 (1st Cir. 2006).

[15] United Catholic Parish Schools of Beaver Dam Educational Ass'n v. Card Services Center, 2001 WI App 229, 248 Wis. 2d 463, 636 N.W.2d 206, 46 U.C.C. Rep. Serv. 2d 754 (Ct. App. 2001).

End of Document

11 Am. Jur. 2d Bills and Notes § 267

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

5. Taking Instrument Without Notice of Claims and Defenses

e. Notice of Defense or Claim in Recoupment

§ 267. Notice of defense or claim in recoupment as affecting status as holder in due course, generally

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 332

To qualify as a holder in due course, a holder must take an instrument without notice that any party has a defense[1] or claim in recoupment described in the Uniform Commercial Code.[2] A holder who takes a check with notice of the maker's defense will be denied the status of a holder in due course.[3]

Comment:

Other Code provisions make a distinction between defenses to the obligation to pay the instrument and claims in recoupment by the maker or drawer that may be asserted to reduce the amount payable on the instrument. Because of this distinction, which was not made in former Article 3, the statute stating the requirements to qualify as a holder in due course refers to both a defense and a claim in recoupment.[4]

The critical time for determining whether a holder had notice of defenses to the payment of an instrument is when the party came into possession of the instrument as a holder.[5]

Footnotes

1 U.C.C. § 3-302(a)(2)(vi)[Rev].
The taker of a note was a holder in due course when it had no notice that there was a defense against the original debtor in that the latter had withheld certain amounts from an escrow account. Dupuis v. Federal Home Loan Mortg. Corp., 879 F. Supp. 139 (D. Me. 1995).
The assignee of a promissory note qualified as a holder in due course because it lacked notice that the underlying loan transaction between a bank customer (the maker), and the bank (the payee) violated state law restricting the circumstances in which a bank may make a loan for the purpose of enabling a customer to purchase stock in a bank. State Street Bank & Trust Co. v. Strawser, 908 F. Supp. 249, 30 U.C.C. Rep. Serv. 2d 477 (M.D. Pa. 1995).

2 U.C.C. § 3-302(a)(2)(vi)[Rev] referring to U.C.C. § 3-305(a)[Rev].

3 Vail Nat. Bank v. Finkelman, 800 P.2d 1342, 13 U.C.C. Rep. Serv. 2d 799 (Colo. App. 1990).
Mortgagors created an issue whether they were defrauded and whether a bank trust company was immune to the mortgagors' fraud defense as a holder in due course, where the mortgagors alleged that the original mortgagee had defrauded them and that the bank trust company, which purchased their mortgages as a trustee under a pooling arrangement, was aware of this fraud at the time of its purchase of the notes so that it was not a holder in due course. James v. Nationsbank Trust Co. (Florida) Nat. Assoc., 639 So. 2d 1031 (Fla. 5th DCA 1994).

4 U.C.C. § 3-302[Rev] Official Comment 2.

5 Wells Fargo Bank NA v. Ferruggio Insurance Services of LA Incorporated, 358 F. Supp. 3d 887, 97 U.C.C. Rep. Serv. 2d 894 (D. Ariz. 2019).

End of Document

11 Am. Jur. 2d Bills and Notes § 268

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

5. Taking Instrument Without Notice of Claims and Defenses

e. Notice of Defense or Claim in Recoupment

§ 268. Notice or knowledge of lack or failure of consideration as affecting status as holder in due course

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 332

One who takes a negotiable instrument knowing that it was issued without consideration takes with notice of a defense of a party to the instrument and is not a holder in due course.[1] Knowledge that consideration for an instrument is illegal prevents one from taking it as a holder in due course,[2] as does full knowledge of the lack or failure of the consideration between the original parties.[3]

A recital of consideration in itself does not constitute notice of a failure of consideration for an instrument,[4] unless the recital makes the instrument conditional on the performance of an executory consideration,[5] in which case the instrument is not negotiable,[6] and then there cannot be a holder in due course.[7]

Footnotes

1 Frequency Electronics, Inc. v. National Radio Co., Inc., 422 F. Supp. 609, 20 U.C.C. Rep. Serv. 680 (S.D. N.Y. 1975), judgment aff'd, 546 F.2d 497, 20 U.C.C. Rep. Serv. 684 (2d Cir. 1976).

2 Hurley v. Union Trust Co. of Rochester, 244 A.D. 590, 280 N.Y.S. 474 (3d Dep't 1935).

3 A. B. G. Inv., Inc. v. Selden, 336 So. 2d 444 (Fla. 4th DCA 1976); Arcanum Nat. Bank v. Hessler, 69 Ohio St. 2d 549, 23 Ohio Op. 3d 468, 433 N.E.2d 204, 33 U.C.C. Rep. Serv. 604 (1982).

4 Jockmus v. Claussen & Knight, 47 F.2d 766 (S.D. Fla. 1930).

[5] First Nat. Bank of Duluth v. School Dist. No. 15 of Carlton County, 173 Minn. 383, 217 N.W. 366, 56 A.L.R. 1369 (1928).

[6] § 76.

[7] § 217.

End of Document

11 Am. Jur. 2d Bills and Notes § 269

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

5. Taking Instrument Without Notice of Claims and Defenses

e. Notice of Defense or Claim in Recoupment

§ 269. Knowledge of separate agreement as affecting status as holder in due course

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 332

A holder in due course is not affected by the terms of a separate written agreement of which the holder lacks notice, even though, as between the obligor and the immediate obligee or a transferee, the terms of another agreement executed as part of the same transaction may modify or affect the terms of the instrument; thus, the rights of the payee are not necessarily the same as those of a holder in due course.[1] For instance, the right of a maker of a note to receive indemnification from the payee under certain circumstances does not make a note voidable and deprive the transferee of holder-in-due-course status.[2]

Footnotes

1 Leasing Service Corp. v. Crane, 804 F.2d 828, 3 U.C.C. Rep. Serv. 2d 329 (4th Cir. 1986); Freitag v. Lakes of Carriage Hills, Inc., 467 So. 2d 708 (Fla. 4th DCA 1985).
As to the effect of a separate agreement on a negotiable instrument, see §§ 111 to 114.

2 First Federal Sav. & Loan Ass'n of Salt Lake City v. Gump & Ayers Real Estate, Inc., 771 P.2d 1096, 9 U.C.C. Rep. Serv. 2d 139 (Utah Ct. App. 1989).

End of Document

11 Am. Jur. 2d Bills and Notes § 270

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

B. Status and Rights of Holder in Due Course

5. Taking Instrument Without Notice of Claims and Defenses

e. Notice of Defense or Claim in Recoupment

§ 270. Notice of discharge of party to instrument as affecting status as holder in due course

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 332

Notice of discharge of a party, other than discharge in an insolvency proceeding, is not notice of a defense, but the discharge is effective against a person who became a holder in due course with notice of it.[1]

Comment:

Discharge is treated separately from the other defenses, notice of which prevents a holder from qualifying as a holder in due course. Except for discharge in an insolvency proceeding, which is specifically stated to be a real defense in U.C.C. § 3-305(a)(1)[Rev], which describes defenses to which even a holder in due course is subject, discharge is not expressed in Article 3 as a defense. Discharge is effective against anybody except a person having rights of a holder in due course who took the instrument without notice of the discharge. Notice of discharge does not disqualify a person from becoming a holder in due course. For example, a check certified after it is negotiated by the payee may subsequently be negotiated to a holder. If the holder had notice that the certification occurred after negotiation by the payee, the holder necessarily had notice of the discharge of the payee as an indorser. Notice of that discharge does not prevent the holder from becoming a holder in due course, but the discharge is effective against the holder. Notice of a defense of a maker, drawer, or acceptor based on a bankruptcy discharge is different. There is no reason to give holder-in-due-course status to a person with notice of that defense.[2]

Footnotes

[1] U.C.C. § 3-302(b)[Rev].

[2] U.C.C. § 3-302[Rev] Official Comment 3.

11 Am. Jur. 2d Bills and Notes VII C Refs.

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

C. Lost, Stolen, or Destroyed Instruments

Topic Summary | Correlation Table

Research References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 363, 443, 488
West's Key Number Digest, Finance, Banking, and Credit 605
West's Key Number Digest, Lost Instruments 1, 13.1, 16, 18, 23

A.L.R. Library

A.L.R. Index, Bills and Notes
A.L.R. Index, Lost or Destroyed Instruments
A.L.R. Index, Uniform Commercial Code (UCC)
West's A.L.R. Digest, Bills and Notes 363, 443, 488
West's A.L.R. Digest, Finance, Banking, and Credit 605
West's A.L.R. Digest, Lost Instruments 1, 13.1, 16, 18, 23

End of Document

11 Am. Jur. 2d Bills and Notes § 271

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

C. Lost, Stolen, or Destroyed Instruments

1. In General

§ 271. Enforcement of negotiable instrument by person not in possession of it, generally

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 443, 488
West's Key Number Digest, Lost Instruments 13.1, 16

A.L.R. Library

Rights of one who acquires lost or stolen traveler's checks, 42 A.L.R.3d 846

Forms

Forms relating to lost or stolen note or instrument, see Am. Jur. Pleading and Practice Forms, Commercial Code [Westlaw®(r) Search Query]

Commercial paper constitutes intangible property and only represents or evidences legal title to, or the right to possess, property of intrinsic value, and neither the value or money or funds it represents, nor the legal right to receive those funds, is "lost" when the paper evidence is lost or destroyed.[1]

The mere absence of a note from the owner's possession does not defeat the owner's right to bring an action to enforce it.[2] A person not in possession of an instrument is entitled to enforce it if:
(1) the person seeking to enforce the instrument was entitled to enforce the instrument when the loss of possession occurred,[3]

or has directly or indirectly acquired ownership of the instrument from a person who was entitled to enforce the instrument when that loss occurred;[4]

(2) the loss of possession was not the result of a transfer by the person or a lawful seizure;[5] and
(3) the person cannot reasonably obtain possession of the instrument because the instrument was destroyed, its whereabouts cannot be determined, or it is in the wrongful possession of an unknown person or a person who cannot be found or is not amenable to service of process.[6]

As a result of the described provision of the Uniform Commercial Code, a failure to produce a promissory note does not prevent the payee's enforcement of the note, in light of evidence establishing the terms of note and its validity as a negotiable instrument.[7]

Comment:

The rights described in the described section of the U.C.C. are those of "a person entitled to enforce the instrument" at the time of loss, rather than those of an "owner" as stated in U.C.C. § 3-804[Rev], which was contained in the prior version of Article 3.[8]

It has been recognized that an owner (now a person entitled to enforce the instrument) may proceed under Article 3 by a direct action against the makers and indorsers on the instrument without first reestablishing the instrument in a separate action.[9] The provision is an exception to the requirement that the suit be brought by a holder and that the holder be a person with possession of the paper.[10] On the other hand, when the plaintiff does not make any claim that a negotiable instrument has been lost or stolen, the provision does not apply.[11]

Observation:

A claimant who is a person entitled to proceed under the section dealing with lost, destroyed, or stolen instruments generally,[12] and is also a person who has the right to assert a claim under the section of the U.C.C. dealing with lost, destroyed, or stolen cashier's, teller's, or certified checks,[13] has the option to proceed under either section.[14]

Footnotes

1 Parker v. Dudley, 527 So. 2d 240, 6 U.C.C. Rep. Serv. 2d 149 (Fla. 5th DCA 1988).
As to rights with respect to lost or destroyed instruments, generally, see Am. Jur. 2d, Lost and Destroyed Instruments §§ 1 et seq.

2 G.E. Capital Mortg. Services, Inc. v. Neely, 135 N.C. App. 187, 519 S.E.2d 553, 39 U.C.C. Rep. Serv. 2d 1170 (1999).

3 U.C.C. § 3-309(a)(1)(A)[Rev].

4 U.C.C. § 3-309(a)(1)(B)[Rev].

[5] U.C.C. § 3-309(a)(2)[Rev].

[6] U.C.C. § 3-309(a)(3)[Rev].

[7] Greenville Riverboat, LLC v. Less, Getz & Lipman, P.L.L.C., 131 F. Supp. 2d 842 (S.D. Miss. 2000).
As to the burden, manner, and standard of proof in an action to enforce a lost, destroyed, or stolen instrument, see § 273.

[8] U.C.C. § 3-309[Rev] Official Comment 1.
Former U.C.C. § 3-804, rather than U.C.C. § 3-309[Rev], applied to a note due prior to the effective date of the latter, since the creditor's rights had accrued by then. Briscoe v. Goodmark Corp., 130 S.W.3d 160 (Tex. App. El Paso 2003).
As to the distinction between a person entitled to enforce an instrument and its owner, see § 206.

[9] Dunn v. Willis, 599 So. 2d 271, 19 U.C.C. Rep. Serv. 2d 826 (Fla. 5th DCA 1992).

[10] Hanalei, BRC Inc. v. Porter, 7 Haw. App. 304, 760 P.2d 676, 7 U.C.C. Rep. Serv. 2d 1528 (1988).
As to the requirement that a holder be in possession of the instrument, see § 206.

[11] Lloyd v. Lawrence, 472 F.2d 313, 11 U.C.C. Rep. Serv. 1205 (5th Cir. 1973).

[12] U.C.C. § 3-309[Rev].

[13] U.C.C. § 3-312[Rev], discussed in §§ 274 to 278.

[14] U.C.C. § 3-312(d)[Rev], discussed in §§ 274 to 278.

End of Document

11 Am. Jur. 2d Bills and Notes § 272

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

C. Lost, Stolen, or Destroyed Instruments

1. In General

§ 272. Providing security to protect defendant in action to enforce lost instrument

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Lost Instruments 18

In a case brought by a person entitled to enforce a lost instrument, the court may not enter judgment in favor of the person seeking enforcement, unless it finds that the person required to pay the instrument is adequately protected against a loss that might occur by reason of a claim by another person to enforce the instrument.[1] Adequate protection may be provided by any reasonable means.[2]

Comment:

A judgment to enforce the instrument may not be given unless the court finds that the defendant will be adequately protected against a claim to the instrument by a holder who may appear at some later time. The court is given discretion in determining how adequate protection is to be assured. Adequate security is a flexible concept. For example, there is a substantial risk that a holder in due course may make a demand for payment if the instrument was payable to bearer when it was lost or stolen. On the other hand, if the instrument was payable to the person who lost the instrument and that person did not indorse it, no other person could be a holder of the instrument. In some cases, there is a risk of loss only if there is doubt about whether the facts alleged by the person who lost the instrument are true. Thus, the type of adequate protection that is reasonable in the circumstances may depend on the degree of certainty about the facts in the case.[3]

Footnotes

1 U.C.C. § 3-309(b)[Rev].

2 U.C.C. § 3-309(b)[Rev].

3 U.C.C. § 3-309[Rev] Official Comment.

End of Document

11 Am. Jur. 2d Bills and Notes § 273

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

C. Lost, Stolen, or Destroyed Instruments

1. In General

§ 273. Burden, manner, and standard of proof in action to enforce lost, destroyed, or stolen instrument

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Lost Instruments 23

A.L.R. Library

Statute excluding testimony of one person because of death of another as applied to testimony in respect of lost or destroyed instrument, 18 A.L.R.3d 606

Trial Strategy

Foundation for Admission of Secondary Evidence, 35 Am. Jur. Proof of Facts 2d 147

A person seeking enforcement of a lost, destroyed, or stolen instrument must prove the terms of the instrument and his or her right to enforce it.[1] Because the plaintiff in such an action is not in possession of the instrument and is technically not a "holder," he or she must prove affirmatively every element essential to recovery on the instrument.[2]

Since a note is not a debt, but only primary evidence of one,[3] an instrument that is lost, impaired, or destroyed may be proved by secondary evidence.[4] A photocopy of a note may be admissible in evidence when it is testified that the copy is a photocopy of the original and that the original has been lost.[5] The creditor's oral testimony may also be received.[6] Under

some authority, a person seeking to enforce a lost instrument may prove the terms of the instrument and the right to enforce it either through a lost note affidavit or by testimony from a person with knowledge.[7]

The party seeking to enforce a lost negotiable instrument establishes a prima facie case by showing the loss of the original, that the copy offered in evidence was a photocopy, and that the signature on the copy was that of the defendant; such a prima facie case is not overcome by a mere denial that the note had been executed or that a demand had not ever been made on the note.[8] The determination of the sufficiency of such proof is largely a matter within the trial court's discretion.[9]

Caution:

Lost-note affidavits are most commonly used to prove the terms of an underlying debt; ?they are rarely enough by themselves to prove ownership of a debt.[10]

Observation:

If the party seeking to enforce a lost, destroyed, or stolen instrument meets the burden of proving the terms of the instrument and the person's right to enforce it, the section of Article 3 governing proof of signatures and status as holder in due course[11] applies to the case as though the person seeking enforcement had produced the instrument.[12]

There has been a conflict of authority concerning whether a plaintiff suing on a lost or stolen instrument is required to produce "satisfactory" proof[13] must establish its entitlement to recover under a lost note by a preponderance of the evidence,[14] or must present evidence that is "clear and convincing."[15]

CUMULATIVE SUPPLEMENT

Cases:

Trial court violated borrower's due process rights when it adjudicated issue of lost original promissory note in lender's action for breach of the promissory note, money lent, and foreclosure of security interest in collateral; lender knew at the time it filed complaint that it did not have original note, lender failed to state in its pleadings that original promissory note was lost and that it intended to reestablish the note pursuant to statute governing enforcement of lost instruments, lender failed to amend its complaint at trial, and issue was not tried by consent. U.S. Const. Amend. 14; Fla. Stat. Ann. § 673.3091. American Residential Equities LLC v. Saint Catherine Holdings Corporation, 306 So. 3d 1057 (Fla. 3d DCA 2020).

[END OF SUPPLEMENT]

Footnotes

1 U.C.C. § 3-309[Rev].

2 Investment Service Co. v. Martin Bros. Container & Timber Products Corp., 255 Or. 192, 465 P.2d 868, 7 U.C.C. Rep. Serv. 373 (1970).
As to the requirement that a holder be in possession of the instrument, see § 206.

3 § 115.

4 New England Sav. Bank v. Bedford Realty Corp., 246 Conn. 594, 717 A.2d 713 (1998); Gutierrez v. Bermudez, 540 So. 2d 888, 9 U.C.C. Rep. Serv. 2d 1310 (Fla. 5th DCA 1989); Aesoph v. Golden, 367 N.W.2d 639 (Minn. Ct. App. 1985); Mitchell Bank v. Schanke, 2004 WI 13, 268 Wis. 2d 571, 676 N.W.2d 849 (2004).

5 Lester v. Groves, 162 Ga. App. 590, 291 S.E.2d 785 (1982); Owen v. Ostrum, 259 Mont. 249, 855 P.2d 1015, 23 U.C.C. Rep. Serv. 2d 614 (1993); Equitable Life Assur. Soc. of U.S. v. Starr, 241 Neb. 609, 489 N.W.2d 857 (1992).
When an original note is not available, an action may be brought on a copy of it. In re A & E Family Investment, LLC, 359 B.R. 249 (Bankr. D. Ariz. 2007).

6 Briscoe v. Goodmark Corp., 130 S.W.3d 160 (Tex. App. El Paso 2003).

7 Wisman v. Nationstar Mortgage, LLC, 239 So. 3d 726 (Fla. 5th DCA 2017).

8 Steven v. Falese Land Co., 50 Ill. App. 3d 231, 8 Ill. Dec. 581, 365 N.E.2d 967 (2d Dist. 1977).

9 Barber v. Ehrich, 394 So. 2d 220, 31 U.C.C. Rep. Serv. 1038 (Fla. 5th DCA 1981); Affiliated Capital Corp. v. Musemeche, 804 S.W.2d 216 (Tex. App. Houston 14th Dist. 1991), writ denied, (Apr. 24, 1991).
The evidence substantially supported a trial court's finding regarding the existence and terms of a lost promissory note, where the payee testified that he had surrendered it to an officer of the corporate maker, the officer testified about the note's execution and his presence then, the payee and officer testified about the note's contents and the fact that no one had been able to find it after its surrender by the payee, and the guarantor of the note did not dispute its existence, but simply stated that he could not recall it. Lutz v. Gatlin, 22 Wash. App. 424, 590 P.2d 359, 26 U.C.C. Rep. Serv. 129 (Div. 3 1979).

10 Cogswell v. CitiFinancial Mortg. Co., Inc., 624 F.3d 395 (7th Cir. 2010) (under Illinois law).

11 U.C.C. § 3-308[Rev], discussed in § 223.

12 U.C.C. § 3-309[Rev].

13 Union Sav. Bank v. Cassing, 691 S.W.2d 513, 41 U.C.C. Rep. Serv. 135 (Mo. Ct. App. W.D. 1985).

14 Secy. of Veterans Affairs v. Leonhardt, 2015-Ohio-931, 29 N.E.3d 1, 86 U.C.C. Rep. Serv. 2d 55 (Ohio Ct. App. 3d Dist. Crawford County 2015).

15 Buster v. Gale, 866 P.2d 837, 24 U.C.C. Rep. Serv. 2d 1164 (Alaska 1994); Fales v. Norine, 263 Neb. 932, 644 N.W.2d 513, 47 U.C.C. Rep. Serv. 2d 1257 (2002).

End of Document

11 Am. Jur. 2d Bills and Notes § 274

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

C. Lost, Stolen, or Destroyed Instruments

2. Cashier's, Teller's, or Certified Check

§ 274. Asserting claim to amount of lost, destroyed, or stolen cashier's check, teller's check, or certified check, generally

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Finance, Banking, and Credit 605

West's Key Number Digest, Lost Instruments 1

Article 3 of the Uniform Commercial Code provides special procedures for asserting a claim to the amount of a lost, destroyed, or stolen cashier's check, teller's check, or certified check.[1]

Observation:

A typical case to which this provision applies is where a customer of a bank closes an account and takes a cashier's check or teller's check of the bank as payment of the amount of the account; in such a case, the check will normally be payable to the customer. In another typical case, a cashier's check or teller's check is bought from a bank for the purpose of paying some obligation of the buyer of the check; in such a case the check may be made payable to the customer and then negotiated to the creditor by indorsement, but often the payee of the check is the creditor. In the latter case, the customer is a "remitter," and the Code provision covers loss of the check by either the remitter or the payee. It also covers a loss of a certified check by either the drawer or payee.[2]

A claimant may assert a claim to the amount of a cashier's, teller's, or certified check that was lost, destroyed, or stolen, by a communication to the obligated bank[3] describing the check with reasonable certainty and requesting payment of the amount of the check if:[4]

(1) the claimant is the drawer or payee of a certified check or the remitter of a cashier's check or teller's check;

(2) the communication contains or is accompanied by a declaration of loss of the claimant with respect to the check;

(3) the communication is received at a time and in a manner affording the bank a reasonable time to act on it before the check is paid; and

(4) the claimant provides reasonable identification, if requested by the obligated bank.

Caution:

An obligated bank against which a claim is made for payment of a lost or missing cashier's, teller's or certified check may not impose requirements beyond those imposed under the Code; for example, the bank may not require the posting of a bond or other form of security where such is not required under the Code.[5]

An indorsee of a certified, cashier's, or teller's check is not covered, because the indorsee is not an original party to the check or a remitter. Limitation to an original party or remitter gives the obligated bank the ability to determine, at the time it becomes obligated on the check, the identity of the persons who can assert a claim with respect to the check. The bank is not faced with having to determine the rights of some person who was not a party to the check at that time or with whom the bank has not dealt. If a cashier's check is issued to the order of the person who purchased it from the bank and that person indorses it to a third person who loses it, the third person may assert rights to enforce the check under the section on lost, destroyed, or stolen instruments,[6] but does not have rights under the section dealing specifically with cashier's checks.[7]

A claimant who has the right to assert a claim under the section dealing with lost, destroyed, or stolen cashier's, teller's, or certified checks is also a person entitled to enforce such a check, so as to be entitled to proceed under the section dealing with lost, destroyed, or stolen instruments generally[8] has the option to proceed under either section.[9]

Comment:

Under the section dealing with lost, destroyed, or stolen instruments generally, a person seeking to enforce a cashier's check or teller's check may be required by the court to give adequate protection to the issuing bank against a loss that might occur by reason of the claim by another person to enforce the check.[10] This might require the posting of an expensive bond for the amount of the check.[11]

Footnotes

1 U.C.C. § 3-312[Rev].
A cashier's check, like all commercial paper, only represents or evidences legal title to some property of intrinsic value, and that right is not lost if the paper evidence is lost or destroyed; in this way, a cashier's check, like traveler's checks and money orders, is better than cash, because loss of the paper is not a loss of the funds the paper represents. Parker v. Dudley, 527 So. 2d 240, 6 U.C.C. Rep. Serv. 2d 149 (Fla. 5th DCA 1988).
As to the definitions of cashier's, teller's, and certified checks, see § 32.

[2] U.C.C. § 3-312[Rev] Official Comment 1.

[3] An "obligated bank" means the issuer of a cashier's check or teller's check, or the acceptor of a certified check. U.C.C. § 3-312(a)(4)[Rev].

[4] U.C.C. § 3-312(b)[Rev].
As to the requirement of a declaration of loss, see § 275.

[5] U.C.C. § 3-312[Rev] Official Comment 2.

[6] U.C.C. § 3-309[Rev], discussed in §§ 271 to 278.

[7] U.C.C. § 3-312[Rev] Official Comment 2.

[8] U.C.C. § 3-309[Rev], discussed in §§ 271 to 278.

[9] U.C.C. § 3-312(d)[Rev].

[10] § 272.

[11] U.C.C. § 3-312[Rev] Official Comment 1.

End of Document

11 Am. Jur. 2d Bills and Notes § 275

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes
Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

C. Lost, Stolen, or Destroyed Instruments

2. Cashier's, Teller's, or Certified Check

§ 275. Declaration of loss of cashier's check, teller's check, or certified check

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Finance, Banking, and Credit 605

West's Key Number Digest, Lost Instruments 1

The declaration of loss required when a cashier's, teller's, or certified check is lost is a statement, made in a record under penalty of perjury, to the effect that:[1]

(1) the declarer lost possession of the check;

(2) the declarer is the drawer or payee of the check (in the case of a certified check), or the remitter or payee of the check (in the case of a cashier's check or teller's check);

(3) the loss of possession was not the result of a transfer by the declarer or a lawful seizure; and

(4) the declarer cannot reasonably obtain possession of the check because the check was destroyed, its whereabouts cannot be determined, or it is in the wrongful possession of an unknown person or a person that cannot be found or is not amenable to service of process.

Delivery of a declaration of loss is a warranty of the truth of the statements made in the declaration.[2]

Comment:

The warranty is made to the obligated bank and anybody who has a right to enforce the check. If the declaration of loss falsely alleges the loss of a cashier's check that did not in fact occur, a holder of the check who was unable to obtain payment because the statute caused the bank to dishonor the check would have a cause of action against the declarer for breach of warranty.[3]

Footnotes

1 U.C.C. § 3-312(a)(3)[Rev].
As to the definition of "record," see § 4.

2 U.C.C. § 3-312(b)[Rev].

3 U.C.C. § 3-312[Rev] Official Comment 2.

End of Document

11 Am. Jur. 2d Bills and Notes § 276

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

C. Lost, Stolen, or Destroyed Instruments

2. Cashier's, Teller's, or Certified Check

§ 276. Effect of claim for payment of missing teller's check, cashier's check, or certified check; date enforceable

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Finance, Banking, and Credit 605

West's Key Number Digest, Lost Instruments 1

If a claim for payment of a missing teller's check, cashier's check, or certified check is asserted in compliance with the Uniform Commercial Code, the claim becomes enforceable at the later of:[1]

• the time the claim is asserted

• the 90th day following the date of the check, in the case of a cashier's check or teller's check

• the 90th day following acceptance, in the case of a certified check

Until the claim becomes enforceable, it does not have legal effect, and the obligated bank may pay the check, or, in the case of a teller's check, permit the drawee to pay the check; payment to a person entitled to enforce the check discharges all liability of the obligated bank with respect to the check.[2] If the claim becomes enforceable before the check is presented for payment, the obligated bank is not obliged to pay the check.[3]

Comment:

A claim asserted under the statute does not have any legal effect until the date it becomes enforceable, which cannot be earlier than 90 days after the date of a cashier's check or teller's check or 90 days after the date of acceptance of a certified check. Thus, if a lost check is presented for payment within the 90-day period, the bank may pay a person entitled to enforce the check without regard to the claim and is discharged of all liability with respect to the check. This procedure ensures the continued utility of cashier's checks, teller's checks, and certified checks as cash equivalents. Virtually all such checks are presented for payment within 90 days.[4]

When the claim becomes enforceable, the obligated bank becomes obliged to pay the amount of the check to the claimant, if payment of the check has not been made to a person entitled to enforce the check.[5]

Comment:

If the claim becomes enforceable and payment has not been made to a person entitled to enforce the check, the bank becomes obligated to pay the amount of the check to the claimant. When the bank becomes obligated to pay the amount of the check to the claimant, the bank is relieved of its obligation to pay the check. Thus, any person entitled to enforce the check, including even a holder in due course, loses the right to enforce the check after a claim becomes enforceable.[6]

Footnotes

1 U.C.C. § 3-312(b)(1)[Rev].

2 U.C.C. § 3-312(b)(2)[Rev].

3 U.C.C. § 3-312(b)(3)[Rev].

4 U.C.C. § 3-312[Rev] Official Comment 3.

5 U.C.C. § 3-312(b)(4)[Rev].

6 U.C.C. § 3-312[Rev] Official Comment 3.

End of Document

11 Am. Jur. 2d Bills and Notes § 277

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

C. Lost, Stolen, or Destroyed Instruments

2. Cashier's, Teller's, or Certified Check

§ 277. Effect of payment of claim for payment of missing teller's check, cashier's check, or certified check; discharge of bank

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Finance, Banking, and Credit 605

West's Key Number Digest, Lost Instruments 1

Subject to the provision on the payor bank's responsibility for the late return of an instrument,[1] payment to the claimant discharges all liability of the obligated bank with respect to a lost cashier's, teller's, or certified check.[2]

Comment:

An obligated bank that pays the amount of a check to a claimant is discharged of all liability on the check, as long as the assertion of the claim meets the requirements of the governing section of the U.C.C. This release from liability is important in cases of fraudulent declarations of loss. For example, if the claimant falsely alleges a loss that in fact did not occur, the bank, as long as it acts in good faith, may rely on the declaration of loss. On the other hand, a claim may be asserted only by a person described in the statute. Thus, the bank is discharged only if it pays such a person. Although it is highly unlikely, it is possible that more than one person could assert a claim to the amount of a check. Such a case could occur if one of the claimants makes a false declaration of loss. The obligated bank is not required to determine whether a claimant who complies with the statute is acting wrongfully. The bank may utilize procedures outside Article 3, such as interpleader, under which the conflicting claims may be adjudicated.[3]

The only exception to the rule discharging the bank of all liability is the unlikely case in which the obligated bank subsequently incurs liability with respect to the check under the provision in Article 4 relating to a payor bank's responsibility for the late return of an item. For example, Obligated Bank is the issuer of a cashier's check and, after a claim becomes enforceable, it pays the claimant under Article 3. Later the check is presented to Obligated Bank for payment over the counter. Under Article 3, Obligated Bank is not obliged to pay the check and may dishonor the check by returning it to the person who presented it for payment. But the normal rules of check collection are not affected by the section in Article 3 governing missing cashier's checks. If Obligated Bank retains the check beyond midnight of the day of presentment without settling for it, it becomes accountable for the amount of

the check under Article 4, even though it had no obligation to pay the check.[4]

Footnotes

1 U.C.C. § 4-302(a)(1)[Rev], discussed in § 314.

2 U.C.C. § 3-312(b)(4)[Rev].

3 U.C.C. § 3-312[Rev] Official Comment 3.

4 U.C.C. § 3-312[Rev] Official Comment 3.

11 Am. Jur. 2d Bills and Notes § 278

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

VII. Persons Entitled to Enforce Instruments; Status and Rights of Holder or Transferee

C. Lost, Stolen, or Destroyed Instruments

2. Cashier's, Teller's, or Certified Check

§ 278. Rights of bank and holder following payment to claimant on missing teller's check, cashier's check, or certified check

Topic Summary | Correlation Table | References

West's Key Number Digest

West's Key Number Digest, Bills and Notes 363
West's Key Number Digest, Finance, Banking, and Credit 605
West's Key Number Digest, Lost Instruments 1

Under the Article 3 provision on lost checks,[1] the right of a holder in due course to receive payment on a check from a bank is greater than the right of a claimant who has filed a false declaration of loss.[2] If the obligated bank pays the amount of the check to a claimant as required,[3] and the check is presented by a person having rights of a holder in due course, the claimant is obliged to refund the payment to the obligated bank if the check is paid, or pay the amount of the check to the person having rights of a holder in due course if the check is dishonored.[4]

Comment:

Although it is unlikely that a lost check would be presented for payment after the claimant was paid by the bank under Article 3, it is possible for it to happen. Suppose the declaration of loss by the claimant fraudulently alleged a loss that in fact did not occur. If the claimant negotiated the check, presentment for payment would occur shortly after negotiation in almost all cases. Thus, a fraudulent declaration of loss is not likely to occur unless the check is negotiated after the 90-day period has already expired or shortly before expiration. In such a case, the holder of the check, who may not have noticed the date of the check, is not entitled to payment from the obligated bank if the check is presented for payment after the claim becomes enforceable. The remedy of the holder who is denied payment in that case is an action against the claimant under the Code if the holder is a holder in due course, or for breach of warranty. The holder would also have common-law remedies against the claimant under the law of restitution or fraud.[5]

Footnotes

1 U.C.C. § 3-312[Rev].

2 California Golf, L.L.C. v. Cooper, 163 Cal. App. 4th 1053, 78 Cal. Rptr. 3d 153 (2d Dist. 2008).

3 § 276.

4 U.C.C. § 3-312(c)[Rev].

5 U.C.C. § 3-312[Rev] Official Comment 3.